STUDIES IN
DEATH DUTIES

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PREFACE

This book was at first conceived by one of us when in the month of February 1946 a bill to provide for the levy and collection of an estate duty in the provinces of India was introduced in the Central Assembly by the then Finance Member, Sir Archibald Rowlands. Some material was collected and a general outline was also fixed. As the bill was circulated for eliciting public opinion by an executive order, it gave ample time for further collection of data and this period has been utilised to the utmost advantage. Before the actual work could be started, one of us (Mr. Gadgil) was invited to join the Government of India in August 1947. This naturally meant abandonment of the idea but as a result of his association with the other (Mr. Vithal Babu) it was decided that these studies should be completed and the result should be embodied in a modest publication. The opinions so far as they are expressed are entirely those of us and have no relevance to the official capacities of one as the Cabinet Minister and of the other as in the Congress Party in the Parliament of India (Research Section).

The simple object of this publication is firstly to educate the public and to stimulate study of this particular subject in quarters where it has not yet received the attention it deserves. If India of tomorrow is going to be a real democracy, nothing is better calculated to achieve this than a fair and equitable division of national dividend and national wealth. This cannot be achieved by any violent means but only by a proper and a progressive system of taxation. While taxing income during life-time, certain principles are relevant. The taxation must be such as would not hamper the incentive of the individual to earn more and to work more and to save more, whereas the principles that would govern an Estate or an Inheritance Tax must naturally be different. The most relevant consi-

deration here would be to what extent such a taxing would affect saving and investment of capital. We are firmly of the opinion that levying of such a tax is not only equitable but will go a long way to reduce the social bitterness which is a consequence of inequitable division of wealth. We hope that this publication will be found useful by the public at large and of immense value to students of Public Finance.

New Delhi,
January 21st, 1949.

N. V. GADGIL
V. VITHAL BABU

CONTENTS

PREFACE

CHAP. PAGE

1. INTRODUCTION 1

Democracy and Economy. Government and Economy. Classification of Taxes. Characteristics of a Sound System. Taxation as a Fiscal Measure. Taxation as a Social Measure.

2. REDISTRIBUTION OF WEALTH .. 44

Inequality of Incomes from Inborn Gifts and Environment. Inequality of Incomes from Work. Inequality of Incomes from Property. Theories of Distribution and Distributive Justice. National Income and Existing Inequalities. Redistribution of Wealth. Taxation as an Instrument for Redistribution.

3. HISTORY OF DEATH DUTIES .. 82

Death Duties in Ancient and Medieval Times—India, United Kingdom, United States of America, Australia, Canada, U.S.S.R., France, Italy, Germany. Summary.

4. THEORY OF DEATH DUTIES 111

Classification of Death Duties. Characteristics of Estate Duty and Inheritance Tax. Justification of Death Duties. Theories against Death Duties.

5. STRUCTURE OF DEATH DUTIES .. 138

Progression in Rates. Minimum Exemption. Graduation. Consanguinity of the Heir or Relationship Distrimination. Rignano's Scheme of Death Duties. Variant of Rignano's Proposals by Dalton.

United Kingdom. United States of America. Australia. Canada.

6. JURISDICTION AND ADMINISTRATION 178

Jurisdiction of Death Duties. Arguments in Favour of State Jurisdiction. Arguments in Favour of Federal Jurisdiction. Administration of Death Duties. Double Taxation. Evasion and Avoidance. Administration of Death Duties.

7. INCIDENCE AND EFFECTS 197

Incidence. Estate and Legacy Duties. Incidence of Death Duties in Great Britain. Effects of Death Duties. Effects Agriculture. Psychological Effects. Total Effects on Saving and Enterprise. Effects of Legacy and Succession Duties. Effects on Capital. Death Duties Consume Capital. Death Duties and Work and Saving. Social Effects of Death Duties.

8. INTRODUCTION OF DEATH DUTIES .. 216

Laws of Inheritance — Hindu Law, Muslim Law. Constitutional Position of Estate Duties. Succession or Estate Duty. Objects of Estate Duty Bill, 1948. Hindu Code and Estate Duty Bill. Important Sections of Estate Duty Bill.

APPENDIX I. A Bill to Provide for the Levy and Collection of an Estate Duty in the Provinces of India 249

APPENDIX II. Preliminary Report of the Select Committee on the Estate Duty Bill, 1948. 293

CHAPTER 1

INTRODUCTION

DEMOCRACY AND ECONOMY, 2. GOVERNMENT AND ECONOMY, 3. CLASSIFICATION OF TAXES, 4. CHARACTERISTICS OF A SOUND TAX SYSTEM, 5. TAXATION AS A FISCAL MEASURE, 6. TAXATION AS A SOCIAL MEASURE—SUMMARY.

DEMOCRACY AND ECONOMY

Democracy in the modern age has come to be associated with the pursuit of equality of opportunity and full-fledged freedom of action to the majority of the people of a country in all walks of life, with due limitations imposed upon them in the common interest. The four distinct aspects of democracy that have been recognised of late, are political, civil, ethical and economic. These make the complete circle and students of democracy cannot afford to ignore any of them, as the essentials of such an institution are ingrained in all those arcs that a precise connotation of it will be defective otherwise. Political democracy supplies the only form of government, wherein full confidence can safely be preserved and trust reposed. It affords the means for the full expression of the citizen in the formation and execution of the policies of the government and guarantees to him the right to vote, to hold office, to form political parties, and to criticise the governmental machinery, though often unintelligently, and sometimes even mendaciously. *

Liberty, in the constitution of a country under such a type of democracy, remains the birth-right of every citizen and cannot be snatched away even by the head of the government. It is something personal, and the citizen will not be unmindful of the interest of the society

* Wolfe: Economy & Democracy, (American Economic Review)), March 1944.

in his day-to-day activities, for otherwise any excessive exercise of liberty will do more harm than good as a whole. Civil democracy is another vital aspect of democracy. Its basic pillars comprise individual liberty and equality before the law. This inculcates civic consciousness in the citizen and equality is not only accepted as a civic principle and a sacrament, but is also fortified by legal sanctions behind it, and any encroachment on equality can be resisted in a court of law.

The third aspect deals with ethical democracy, which is practically synonymous with, say Christian, Hindu, Muhammedan and other religious canons of ethics. The ethical aspect is the fundamental aspect, as the ethical basis is the ultimate basis. The science of morality shapes this feature of democracy in such a way that individual actions are guided by the respect for that "individualism of ends", which is truly becoming of an institution of government broad-based on high moral codes of conduct. Moral laws seem often to be in conflict with the decisions of the government, Major decisions affecting the well-being of a country as a whole cannot afford to ignore their ethical implications and it is the inherent right of democracy to emphasize this aspect as it makes possible a broader application and interpretation of the fundamental principle of economy.

The fourth facet can be termed economic democracy. Just as political democracy cannot be compatible with a hereditary ruling class, so also economic democracy cannot be reconciled with a hereditary plutocracy.† Great is the relationship between democracy and economy and it can be summed up as one of equality of opportunity, according to Wolfe. ‡ Absolute equality of income cannot be realised, but absolute equality of opportunity is a prerequisite of economic democracy. This is not tantamount

* Stephen Francis Weston: The Principle of Justice in Taxation, (New York, 1903).
† Geoffrey Growther: Economics for Democrats.
‡ Wolfe: Economy & Democracy (American Economic Review, March 1944.)

to the dead level of equal opportunity and great caution should guide us in the pursuit of equality. In any economy, such a rigid level cannot be easily determined. Under no circumstances, would a conclusion in this behalf hold good for all time. In fact, that would result in a reversal of real economy. Equal opportunities should necessarily bear a responsible proportion to the capacity to utilise them. It would be of no avail if merely opportunities were to be afforded equally to all. The ability to make the best of them should at the same time be taken into consideration. Equality of opportunities has therefore to bear an essential relation to various individual abilities.

"To distribute wealth and income, and the opportunity they represent in any other way is patently a violation of the principle of economy, which is to put things where they will do the most good." (Wolfe). Thus, democracy would be constantly working for bringing about the requisite changes in the structure of economy so as not only to afford equality of opportunities but also to justify from the point of view of the greatest good of the largest number of population, any such adjustments it might call for in the processes, say, of the development of the national potentialities, of pursuing an appreciable scale of industrialization and of distributing the national income equitably. Therein lies the freedom of opportunity. It has been often remarked that democracy is perhaps epitomized in the whole modern trend away from rigidity of status to freedom of action and opportunity, which in turn bear the objectives of democratic economy, say, of the abolition of poverty, reduction of inequality and variability of incomes. While working out these objectives, due emphasis should be laid in all these cases, on keeping the efficiency of all factors of production on a high level. If equity alone is the guiding star, it might be that it rapidly makes headway for reducing inequality of wealth, at the cost of total production. So also would such an equity be unattractive and unjustifiable if it ultimately resulted in a dead level of poverty for all. This naturally puts the point clear that

the aspirations of equality should be closely studied for its effects on the country as a whole. Otherwise, the term "democratic economy" would be bereft of its meaning. Thus, any system of economic democracy, which aims at the welfare of all the people in their individual capacities, depends for its success not only on its ends, but also on the means employed.

The connotation of "real democracy" is resonant as it stands for a society dynamic in character and adherent to the canons of social justice and economic equality. It is a framework of a remarkable body of social and economic rights (rest, work, education, racial and sexual equality and religious freedom) which are guaranteed to every citizen.* Equitable diffusion of economic power and an even-decentralization of national wealth are the concomitants of success of such a democratic state. This necessarily presupposes regimentation of economic potentialities in such a way as to further human progress and place the society as a whole within easy reach of the essential requirements of life. Naturally, industrial relations, under these conditions, will not be strained as the employer and the employee will be placed on an 'even keel', as it were, with one another. Lack of such harmonious relationship will surely undermine the foundation of economic democracy. Such an organization will be more successful under conditions of co-partnership and co-sharing of the profits in the business enterprizes so as to instil in the workers the responsibility they owe in maximizing production for use as well as gain and to minimize wastage of materials or loss of time. This will, in due course, regulate the scales of distribution also, as the end and aim of production in an economic democracy centres round the community's interest.

Government and Economy

The type of economy depends none the less upon the form of government and the party in power. If it is a

* Prof. H. L. Laski in Manchester Guardian, "Soviet Russia enlarges bounds of human liberties".

conservative capitalist government, it will be guided beyond doubt by its own narrow class interests, to be achieved by legislative measures and executive decrees. It will inaugurate that form of economy which brings about a flow of wealth or productive resources from the common masses to the privileged classes. If, on the other hand, it is a republican form of government on which the agricultural and labouring classes pitch their hopes to build a movement for the realization of democracy, the system of economy would be quite different. While, in the former case, the capitalistic economy aids the pooling up of wealth in a few pockets and helps a high concentration of economic resources in a minority of people, the latter ploughing a different furrow altogether, will be guided in all its activities by the good of the society at large. In the former case the capitalists invariably pursue their sectional and anti-social interests in trying to further their own end, which generally means the expectation of undue profits. In the other case, productive resources would be utilized without any restriction in such a planned way as to assure in the end maximization of aggregate satisfaction. Under a fascist government, circumstances would vary. Facism all the world over came into power after being "subsidized by the great capitalists and reinforced by the small property-owners, as an instrument of force for suppressing socialism and keeping capitalism in being despite its demonstrated inability to serve the fundamental economic purpose of putting the means of production to effective use for the satisfaction of human needs." *

Thus, it has become an anti-economic and anti-social institution utilized only for militaristic purposes. But all the same, the cardinal tenet of the fascist economy gives sufficient scope for the preservation of private enterprize with the inherent right handed over to the state for supervision and not for administration of industries. The capitalist under fascism has to harness his productive system for

* G. D. H. Cole: Practical Economics.

war purposes and has not the same freedom as he would have under a capitalistic government.

Under the socialist government, as in the U.S.S.R., the economic system is featured by the abolition of private property and the regimentation of the means of production, which belong either to the state, co-operatives or collective farms. In other words, they are the property of individual collective farms and co-operative societies. The bulk of the means of production is thus concentrated in the hands of the state, which is the rightful owner of all land and its resources. To exploit the natural potentialities, the state sets itself to the task of engaging in large-scale and intricate operations which form the basic factor in the general economic fabric of the country. The historic struggle for the control of the state by the middle classes in England, France and the U.S.A. during the 17th and 18th centuries culminated in an economy, based on social equality, in which they were pitched against landed aristocracy. A government pursuing *laissez-faire* policy proposes a minimum of state interference with individual action and its economy will be built upon the private property which would be maintained as a fundamental economic institution. Under a socialist economy, as we have already mentioned, we witness a system of ownership of public utilities, equalization of social opportunities and the abolition of private property much opposite to the scheme of things under a capitalistic economy. Under a Communist government, a maximum of state and a minimum of individual economic functions are prescribed, and production, distribution and consumption are so controlled by the state that they eventually result in the furtherance of the common interests of the society as a whole. Out of all these, it is quite clear that a democratic government alone can stand the test of all time and it will because of its potentialities for securing the greatest good of the greatest number of population which supplants "my good, and that of my class."* Thus, it can be said that different

* Emil Leaderer: The State of the Masses, (New York, 1940).

forms of government nurse and nurture different economies.

The All-India Congress Committee which met on 17th November 1947, in New Delhi, passed a resolution on the Congress objectives, as follows:

> "Our aim should be to evolve a political system which will combine efficiency of administration with individual liberty, and an economic structure, which will yield maximum production without the operation of private monopolies and concentration of wealth and which will create a proper balance between urban and rural economies. Such a social structure can provide an alternative to the acquisitive economy of private capitalism and the regimentation of a totalitarian state." †

This vividly explains the probable character of the government under the new constitution and aims at the establishment of real democracy in India with the aid of a "society based on social justice and equality". The relationship betwen political and economic democracy has been crystallised when the A.I.C.C. announced that "democracy in the modern age necessitates planned central direction as well as decentralisation of political and economic power, in so far as it is compatible with the safety of the state, with efficient production and the cultural progress of the community as a whole." Thus, the goal set before the country is the realization of a true democracy and of an economy based on social justice.

Classification of Taxes

Taxes, can be classified into two heads, direct and indirect. J. S. Mill, who is freqnently quoted by lawyers, defined a direct tax as one "demanded from the very persons who it is intended or desired, should pay it", and an indirect tax as one "demanded from one person in the expectation and intention that he shall indemnify himself at the expense of another."* A direct

† Report of the Economic Programme Committee, published by A.I.C.C.

* J. S. Mill: Principles of Economics, Book V., Chapter IIII.

tax is one which falls where it is intended to fall and an indirect tax is one whose final impact does not necessarily fall where it is considered it should fall.

Below we attempt a detailed study of the proportion of direct to indirect taxation in the most important countries of the world:

(a) *India*

Year	Direct Tax	Indirect Tax
1937–38	21%	79%
1938–39	22%	78%
1939–40	20%	80%
1940–41	30%	70%
1941–42	38%	62%
1942–43	60%	40%
1943–44	65%	35%
1944–45	65%	35%
1945–46	53%	47%
1946–47	47%	53%
1947–48 R.E.	52%	48%
1948–49 B.E.	44%	56%

From these figures it is clear that while in 1937-38 direct taxation in India accounted only for 21% of the total revenue, the bulk of taxation was indirect. This proportion varied from time to time till during 1942-43, the change was in favour of direct taxation, as it yielded 60% of the revenue. But that proportion has fluctuated since then and from 1945-46, it appears that effort is being made for the maintenance of a proper balance between direct and indirect taxes.

Mr. Layton's report to the Indian Statutory Commission (1930) embodied some general considerations in these words : "On theoretical grounds, direct taxes have great economic advantages over indirect. Their incidence can be more definitely determined, and they are economical to the taxpayer in the sense that he is not called upon to pay more than the Government receives, and they are

usually inexpensive to collect. But it is impossible to press this theory far in an agricultural country such as India, where a large population is living on a low standard, and where much of the wealth that is accumulated is not in a form in which it can be readily assessed and taxed. In such circumstances, the greater portion of the revenue must be raised by indirect taxes, and fiscal theory must be sacrificed to the necessities of the case. At the same time, these conditions make it even more important than elsewhere that taxation should be adjusted to ability to pay, which means that as large a part of the additional burden as possible should be placed on the richer classes by means of direct taxation".*

Yet it cannot but be said that since 1930, the economic fabric of the country has undergone vital changes for the better. Not only have the central revenues expanded but the provincial revenues have also reached such heights that the total tax revenue yield became substantial. Progressive rates on income-tax contributed nearly 54.5% of the total tax revenue of the country while the remaining was obviously collected from taxes on consumption, such as customs, excise, etc.

The finance Minister, Sir R. K. Shanmukham Chetty, during his budget speech for 1948-49 elaborately dwelt upon the question of the balance between direct and indirect taxes in the Indian tax structure:

> "While in an industrially advanced country, it may be possible to raise a substantial revenue by direct taxation, it will obviously be unwise to pitch the direct taxes too high in a country in the process of development as the inevitable effect of high direct taxation is to retard the formation of capital without which industrial development is not possible. Similarly, when the main consideration is to curtail consumption, as during a period of shortage of goods and inflation, it may be necessary to raise the level of indirect taxation to secure

* Report of the Indian Statutory Commission—(Mr. Layton's Report).

a reduction in consumption. There is also a common fallacy that the larger the amount of indirect taxation the heavier the burden on the ordinary man. While it is of course true that over a considerable field consumption taxes reach a wider section of the population than direct taxation, consumption taxes on such luxuries as motor cars, the costlier varieties of tobacco and cigarettes, duties on wines and spirits, export duties which do not affect the internal consumer, all of which go to swell the total of indirect taxation do not touch the life of the ordinary man.....

"It would be interesting to compare our position in this respect with the United Kingdom. In a highly industrialised country like the United Kingdom, the scope for raising large revenues from direct taxation is greater. The United Kingdom budget for 1947-48 discloses that in that country the percentage of direct taxes to the total tax revenue is only 52. This compares very favourably with our tax structure in which, with a comparatively poor industrial economy, we collect about 51 per cent. of our taxes from direct taxes. Another interesting feature of our economy is that, as compared with 1937-38, the direct taxes would have increased eight and a half times in 1948-49 while the indirect taxes would have increased only by a little over twice. Considering the relatively undeveloped state of our country, I do not think that any one could say that the burden of direct taxation is unduly light or that there has been any shifting of the burden on the shoulders of the ordinary man."*

Admitting that the burden of taxation is not "unduly light", does not necessarily mean that we should be satisfied with direct taxes alone without taxing inheritances, laying stress, of course, on the argument that the burden of taxation should be so distributed between the various groups and so levied upon industries as to cause the best

* Government of India, Part B of Budget speech for 1948-49 pp. 8-9.

dilution, in strict conformity with equity, of the taxpayer's incentive to work and ability to save.

(b) *United Kingdom*

In the U.K., income-tax, sur-tax, death duties, Excess Profits Tax and Profits tax, constitute the fabric of direct taxes; and customs and excise, stamps, etc., comprise indirect taxes. The proportion between direct and indirect taxation was as follows:

Year	Direct	Indirect
1938-39	56%	44%
1944-45	64%	36%
1947-48 (R.E.)	51%	49%
1948-49 (B.E.)	48%	52%

The revenue position of 1947-48 indicates that nearly 51% of the revenue is derived from direct and 49% from indirect taxes, whereas according to the budget estimates of 1948-49, 48% of the revenue will be derived from direct taxes and the balance from indirect taxes. This compares unfavourably with the peak percentage of direct taxation during 1944-45 when it was 64. In a highly industrialized country like the U.K., the proportion of direct to indirect taxes seems to be on the decline, while taxes on consumption seem to be bringing into the exchequer more and more revenue. Speaking over the budget proposals (1948-49), Miss Bacon, M.P. said: "Many theorists in days gone by thought that direct taxation was the best way. . . . (They) . . . believe that direct taxes were right and indirect taxes were wrong. . Contrary to all theories, men and women seem to prefer indirect taxes. They seem to like to get what they earn and to have an element of choice in the spending of it. In the past few years, this direct burden of income tax—the huge sum taken out of wages earned—has caused more grumbling and discontent and lessening of effort by the people than anything else. . . . They resent the unimaginative and unchallengable lopping

off of nearly half a week's salary by some soulless Shylock whom they seem to confuse with the Chancellor of Exchequer, always thirsting for his pound of flesh"..She added: "First, direct taxation must still be the chief form of taxation on large incomes, and. secondly, there must be no indirect taxation of basic necessities, otherwise the old age pensioner and the low-income person are going to be the ones to suffer. I believe, that one of the best features of the Government's policy today is that, although we have indirect taxation, we have also a system of indirect bonuses....."*

(c) *United States of America*

In the U.S.A., the revenue system as a whole can not be said to be either very progressive or regressive, but it is tending to become more and more progressive. The former statement does not hold equal weight in respect to all the Governments, Federal, State and Local. Federal system is by far the more progressive than in many other countries. The Federal Government mainly depends upon income, estate and gift taxes of all kinds and on taxes on business, which accounted for nearly 53% of the federal tax revenues in 1937-38. Taxes on property comprised 36% of the total tax revenue and proved a very important source of revenue in that year and the division of consumption taxes comprised 39% of total tax revenues. Nearly 12% of state revenue was derived from progressive taxes like those on income, estate and gift, and 67% was from consumption taxes. Other taxes on business brought in 13% and the general property tax contributed 8% to the treasury. Thus, there is a great deal of progression in the case of Federal than in the case of State taxes.

* Parliamentary Debates (Hansard), 7th April, 1948.

The proportion between direct and indirect taxes is revealed in this Table:

Year	Direct	Indirect
1938-39	47%	53%
1943-44	78%	22%
1946-47 (Est.)	67%	33%
1947-48 (Est.)	69%	31%

Direct taxes on individuals and on corporations constitute the bulk of the Federal revenues. On the eve of the Second World War, direct taxes which accounted for nearly 47% of the total revenue, increased considerably: they were responsible for nearly 78% in 1943-44, 67% in 1946-47 (R.E.) and 69% in 1947-48 (B.E.).

It will be seen that progressive taxes form the backbone of the federal tax structure. The extraordinary tax measures adopted during the years of war are still being maintained in the United States of America to combat inflation. The result is a very well-balanced tax programme. This not only absorbed some of the additional purchasing power of the consuming public and some of the additional fund which accrued to business from increased consumers' expenditure, but also preserved the anti-inflationary character of taxation which meant excessive rates, that (especially) were borne by individuals without any undesirable economic repercussions. "Tax simplification to reduce the burdens of compliance of the money...to tax payers, by elimination of return where feasible and by other measures are recommended, provided such changes do not result in substantial impairment of receipts for the Treasury or of equity for the tax payers." *

The proportion between direct and indirect taxes is becoming of a much resourceful country like the United States and, reflects the degree of economic justice in placing the tax burden on the shoulders of those with

* United States Budget Speech delivered by President Roosevelt, 1945.

the "broadest backs." The consumption taxes which figure less prominently in the American revenue system provide a redeeming feature inasmuch as those taxpayers with low incomes need not bear a proportionately heavier burden that might ultimately affect the willingness and the capacity to work, as well as to save.

(d) *Canada*

The tax system of Canada was also predominantly regressive. The Dominion Government found the most productive source in sales taxes, which was a conspicuous feature of the Canadian tax system. Before 1939 nearly $138 million accrued from sales tax out of a total of $465 million. The other sources were: $112 million from customs and $52 million from excise.

The following figures tell a different story:—

Year	Direct	Indirect
1937-38	28%	72%
1943-44	53%	47%
1945-46	45%	55%

Although taxation was regressive before the Second War, it was so adjusted later on that it brought in substantial revenue from direct taxes. Its peak percentage of 53 in 1943-44 cannot be favourably compared with similar figures of direct taxation during the War in other countries. Sales tax which previously used to top the list, had to yield place to income and excess profits tax, though it could bring in more revenue than customs and excise. Direct taxation was not pitched sufficiently high, and the Canadian tax structure for that reason was much regressive. Even before the cessation of hostilities, the proportion was once again in favour of indirect taxation.

(e) *Australia*

The Australian revenue system is noted for its regressive policy which is the most conspicuous feature of

the fiscal fabric of the Commonwealth Government. But contrary to this, the States, or the component units of the Commonwealth, embody a progressive element in their revenue system. *

Let us have an idea about the proportion of direct to indirect taxes in the Australian revenue:

Year	Direct	Indirect
1938-39	23%	77%
1943-44	69%	31%
1946-47	53%	47%
1947-48 (B.E.)	63%	37%

These figures show that before the War the revenue yield from taxes on income, estate duty, and land tax was nearly 23%, while customs, excise and sales tax were responsible for the bulk of the total tax revenue. In 1938-39, revenue from customs amounted to nearly 42%, from excise 22%, from income-tax 16% and from estate duty 3% of the total collections. But with the opening of international hostilities and the consequent dire necessity for greater revenue resources, higher and higher degrees of progression were introduced in the field of direct taxes, with the result that the mal-adjustments in the tax programme were corrected. The increased revenue from direct taxes was sumptuous as it brought 69% in 1943-44, 53% in 1946-47 and 63% in 1947-48 (B.E.). We find that the receipts from income tax (including war-time and super tax) were to the tune of £183,799,000 in 1943-44, £153,764,000 in 1946-47 and £1,42,000,000 in 1947-48 (Estimates), as against the pre-war meagre contribution of £11,882,000. Thus, the previous position was completely changed.

(f) *U.S.S.R.*

U.S.S.R. has a different tale to tell altogether. The socialist economic system is the foundation of U.S.S.R.

* Findlay Shirras: Federal Finance in Peace and War.

and it is reflected in the abolition of private property in the means of production, which belong either to the State, co-operatives or co-operative farms. Under the Soviet system taxes not only help accumulating budgetary resources but also serve as an instrument of economic and social policy. The most redeeming characteristic in the fiscal system of U.S.S.R. is that the lion's share of the Union's income is derived from socialist industries and enterprizes, and not from taxes which is in strict conformity with the socialist economic order. Taxation on industrial incomes which plays such a vital role in the financial structure of other countries with a virtually different socio-economic structure is but of minor importance in the socialist economy. In 1937, for instance, when the second Five-Year Plan was completed, and the socialist economic system was fully consolidated, 91.9% of the aggregate revenue accrued from the profits and accumulation of socialist enterprizes, whereas taxes and levies brought in only 8.1%. In 1940 also, no less than 90% of all the budgetary revenue was provided by income from socialist industry, while the income-tax and levies yielded only 10.%.

The relative proportions of the revenue derived from socialist industry and that from taxation during the latest years is analysed here:

Year	Revenue from socialist industries	Revenue from taxes
1937	91.9%	8.1%
1947	94%	7%
1948	93%	7%

That is exactly the reason why Deputy Khokhlov, presenting the report of his budget commission in the Soviet of Nationalities, pointed out that nearly nine-tenths of all the budget revenue has been accruing from socialist

* In the Land of Socialism, by M. I. Bogolepov, V. Betov, N. Alexandrov, M. S. Lipetsker, G. M. Sverdlov, Z. Mokhov, N. Semaskko.

economy, while the share of the payments by the population in the shape of tax and levies has been going down. "Taxes and other revenue from the population, despite the fact that they account for a negligible share in the budget, are of great political significance" and "affect the interests of wide strata of the working people," said Deputy A. G. Zverev, Minister of Finance of the U.S.S.R. on 2nd January, 1948. *

Characteristics of a Sound Tax System

A sound tax system should possess the characteristics of equity, tax adequacy, simplicity, certainty and economy in administration and compliance, economic soundness, and inherent flexibility. †

Equity

For a tax to be just, it should be fair and equitable, and which is one of the most sovereign standards to which any sound tax system should conform. Adam Smith, the father of Political Economy, wrote: "The subjects of every state ought to contribute towards the support of the government, as nearly as possible, in proportion to their respective abilities; that is, in proportion to the revenue which they respectively enjoy under the protection of the state." This has left room for misgivings, for, in his own words, "in proportion to their respective abilities", did not take into careful consideration the respective abilities of the taxpayers, as we have already noticed that the marginal income of a poor man is much less than that of a rich man. ‡ If both of them pay a tax "in proportion to their

* Moscow News, 4 February, 1948.

† Hansen and Perloff: State and Local Finance in National Economy.

‡ "The utility of the last pound diminishes rather rapidly in the early increments of income after the essential needs of life have been satisfied; then the rate of diminution tends to be slower, as the distinction between bare sufficiency and elementary comfort gives way to the slighter distinctions between lesser and greater comfort, and between comfort and luxury."—Report of the Committee on National Debt and Taxation, para. 332.

respective abilities" the principle of tax justice will no longer be in operation.

In another place, Adam Smith observed that "it is not very unreasonable that the rich should contribute to the public expense, not only in proportion to their revenue, but something more than in that proportion." Definitely, this made matters clear, for under the principle of progression, lies the fundamental economic test of taxation, ability to pay, which means that the marginal utility of income grows less and less as incomes increase. Equal taxes do not necessarily impose equal burdens, as the economic conditions of different taxpayers vary.

Economic strength of a society can be revealed from a study of its ability to pay the taxes. The most dependable test for the measure of ability to pay taxes is the size of the income, and the taxable capacity of the individual increases directly in proportion to his income. That the recepients of larger incomes should pay taxes on a progressive scale than those with smaller incomes is recognized as a basic equity in taxation. It necessarily leads to the exemption of incomes which fall below a certain level, as their recepients are supposed to have no ability to pay and hence be exempt from taxation. In addition, distinction is also made between earned and unearned incomes. The former is a direct compensation for personal effort, while the latter is a payment on capital which other persons had accumulated.* There is a strong case for a greater progressive tax to be imposed on the latter rather than on the former since the taxpayers with smaller incomes depend almost entirely on their earned incomes. It is usually argued that unearned incomes are more unequally distributed than earned incomes, and that they can be characterised as "unexpected" and "undeserved".

"The most practicable plan of taxing unearned incomes more heavily than earned ones is to levy a tax with progressive rates, for it automatically taxes funded incomes

* Buchler: Public Finance.

at higher rates as the funded portion increases." But earned incomes should not be so heavily taxed as unearned incomes. Thus, the equity of burden is greatly realized under conditions of progression. The distinction may often be difficult to follow, as most of the tax-payers receive earned as well as unearned incomes. All the same, the argument aids us to observe that in the case of direct taxes alone, we can pursue this differentiation, as in the case of income-tax, death duties, corporation tax, etc., while in the case of indirect taxes, it will be impossible either to make distinction or to levy taxes on the ideal of fairness extending in its application so as to obtain equity in tax burdens as between individuals with varying incomes and individuals under different economic circumstances. While direct taxes fall on those with the ability to bear the tax load, indirect taxes are imposed without any reference to the same principle. Thus while tax burden is equitable in the former case, it might be inequitable and, in fact, "regressive" in the latter. If more equitable taxation is to be attained, we should also have a long-range view of social consequences of the tax system.

Tax Adequacy

History of taxation is a continuous struggle for adequate revenues to meet political, economic and social expediencies. The tax system should not only be equitable in the sense that it be based upon the idea of "plucking the feathers fom the geese which do the least squawking", but should also provide an adequate yield. This is not tantamount to any undermining of the economic system to utilise to the fullest extent the tax system. It naturally owes its success to the breadth of the tax base, national income and other economic phenomenon. The productivity of direct taxes cannot be challenged, as it is quite substantial and equitably realised.

Broadening the tax base equitably with due recognition of tax adequacy depends upon the skill of the Finance

Minister. The proportion of direct to indirect taxation can be adjusted at will by the Finance Minister and tax adequacy is wholly based upon the leap taken by him. But it cannot be denied that greater possibilities for adequately expanding the tax revenue are inherent in direct taxes rather than in the indirect. The principle of progression that affords a great opportunity for increasing tax revenue, would surely stand the test of tax adequacy and could be better utilized in direct rather than indirect taxes. Although figures in certain cases may prove exactly the opposite, that does not destroy the thesis that direct taxes are capable of yielding substantially more revenue.

Simplicity, Certainty and Economy in Administration and Compliance

The tax system should be simple and economical in administration and in compliance. The taxpayers should be certain about the payment: its method, time and the amount. The collection of taxes should not entail a great deal of expenditure either in administration or in compliance. On the other hand, "multiplication, duplication and uncertainty" bring in their trail "irritation, tax-resistance and litigation". In the case of direct taxes, particularly income tax, these characteristics abound. The tax is to be collected at the source. The income tax payer knows how much he has to pay, when he has to pay and as such it does not involve any great complication for him. Avoidance and evasion are impossible and economy in administration and compliance can be easily achieved. But it is not the same case with indirect taxes. Though indirect tax lies concealed within the price of the taxed commodity, and though the taxpayer is not aware of the fact that he is also paying a levy on the goods he is purchasing, all the same, indirect taxes as a whole do not satisfy all the conditions mentioned above.

Economic Soundness

Now we come to another important principle of a well-designed tax system. According to Hansen and Perloff, "the tax system should be devised so as to minimize obstacles to economic progress and maximize economic stability." * Productivity of the tax system is not therefore the only criterion, but it must also produce beneficial effects on the economy of the country as a whole, say by the prevention of tax barriers and thereby promoting the free flow of commodities from one end, of the country to another. Public authorities can also utilize this tax device with a view to fostering local industries. "Tax system should be geared to a rational fiscal policy aimed at economic expansion and cyclical stability. It should tap mass purchasing power at a minimum, except when inflationary developments are threatening. A progressive tax structure serves to facilitate more equitable distribution of income and thereby to develop a high level of consumption." †

Inherent Flexibility

A tax system should be inherently as flexible as possible and should be capable of ready adjustment to the ever-changing conditions in the dynamic economy of a democratic society. The tax structure as a whole should be so broad-based that any major demands should be automatically met with. Such rapid adjustments are quite possible in the field of direct taxation, for, if income taxes loom large in the fiscal system of a country, there will be an automatic draining off of purchasing power as incomes rise, and a smaller drain on purchasing power as incomes fall. Also, if the income tax is on a

* Hansen and Perloff: State and Local Finance in National Economy.

† Financial and Economic Statement, presented on 6th April 1948, in House of Commons by Sir Stafford Cripps.

current, pay-as-you-go basis, changes in economic conditions will immediately be reflected in tax collection."* In direct taxes, where the principle of progression can be pursued with the greatest ease and facility, there is an opportunity for a very high order of flexibility.

It is an intricate question to answer as to what is justice in taxation and no categorical reply can be given, as it is relative to the standards of justice in the community, the economic, political and social set-up of the country, the flexibility of financial resources, the probable effects of public expenditure and several other factors. As the standards of tax justice have to be tempered with the fluctuating conditions, that tax system is the most just which apportions the tax burdens equitably in a manner most conducive to the development of the productive resources of the country. Justice in taxation not only means fiscal justice in as much as the distribution of the tax burden should be in accordance with the relative economic strengths of the tax-payers, but it also includes social justice in so far as it affords the least resistance to the social income and taps the required revenue with the least socially detrimental effects. Any classification of taxes under two broad heads, direct and indirect, would involve a study of the incidence of taxation per capita. The burden may be either money burden or real burden, direct or indirect. The aggregate money burden of a tax relates to its money yield to the public treasury, while its real burden means the sacrifice involved in paying it. In the former case, it represents the total amount of money which would have been left in the pockets of the people to "fructify" as it were, as Gladstone put it, and could have been utilized in purcasing more goods or engaging more services either for consumption or for production; while in the latter case it reflects the real sacrifice of economic welfare which an individual would have acquired had it not been for the

* Hansen and Perloff: State and Local Finance in National Economy.

tax on the commodities. A tax on a commodity does not leave the price unchanged, and when the price increases by the full amount of the tax, the real burden on different tax payers would naturally vary. In both the cases, the marginal rupee results in greater sacrifice to the poor rather than to the rich. As the margin of incomes of different classes of people varies, so would their relative abilities to bear the brunt of any change in taxation. The indirect money burden, on the other hand, refers to the loss of interest on the part of the tax-payer, as he might have paid the tax long before the taxed commodity could be sold and to that extent he might have been out of pocket by the amount of interest. The indirect burden is concerned with the real sacrifice in terms of foregoing or stinting that much of economic welfare which the individual tax-payer would have obtained but for the increase in the price of a commodity due to the tax levy, as its price might be so exorbitant that it might not be within the reach of each and every tax-payer.*

Taxation as a Fiscal Measure

"The older English writers", says Adams, "did not need a theory of expenditures, because the theory of government which held implied a fixed limit to governmental functions."† This belief, however, could not hold good for all time and a tendency both towards an "extensive" as well as an "intensive" increase in the state activities, has persisted under the impulse of democracy with the result that governments have been undertaking more and more functions on an elaborate scale. This has been very clearly exemplified in Wagner's "law of increasing state activities." Wagner declares: "Comparison of the past and present situation of different countries shows that among

* "The equitable distribution of taxation involves the insoluble problem of incidence"—Report of Sir Edward Hamilton and Sir G. Munseny in Royal Commission on Local Taxation, 1901, p. 109.

† Adams : Science of Public Finance, p. 53.

progressive peoples, an increase regularly takes place in the activity of both the central and local governments. The increase is both extensive and intensive; the central and local governments constantly undertake new functions; while performing both old and new functions more efficiently and completely..."† The expansion in governmental functions has been witnessed among democracies, monarchies and dictatorships and is not a little due to the tide of social action, running so swift and so strong. Wars brought in their trail an undreamt of expenditure and the mad race for piling armaments demanded huge additional revenues. Consequently there was an appreciable contraction in the amount expended for social good. All the same, the manifold state activities require substantial revenues and raising them demands great financial acumen.

With the expansion of governmental activities, more revenues had to be collected and they have been derived chiefly from taxes. Taxation, unlike the ones in the 17th and 18th centuries, became a popular and powerful instrument in the hands of the modern governments. The odium it invoked earlier and the prejudiced accusations of several, (philosophic anarchists) who thought that taxation was never morally justifiable and that all public expenditure which had been met by increased sources of revenue through taxation was "unproductive", have all disappeared.

The most conspicuous feature of the fiscal systems of modern times is the supply drawn by the public exchequer from the tax yield. In India for instance, the aggregate revenue of the Central Government can be divided under two heads: tax-revenue and non-tax revenue. The former provides the sheet-anchor of the finances and comprises income-tax, corporation tax, central excise, customs, salt, opium and other miscellaneous items, while the proceeds from non-tax revenue

† Adolph Wagner: **Allgemeine oder theoretische Volkswirtschaftslehre**, Vol. I, **Grundlegung**, p. 260.

consist of the revenue from Railways, Posts & Telegraphs, Irrigation, Currency and Mint, and others. The following table shows how the total revenue has increased since 1937-38.

(Rs. in lakhs)

Year	Total Revenue	Total Tax Revenue
1937-38	1,22,48	74,25
1938-39	1,21,07	73,60
1939-40	1,25,77	80,31
1940-41	1,45,13	76,70
1941-42	1,73,70	97,54
1942-43	2,35,37	1,24,43
1943-44	3,02,87	1,70,29
1944-45	3,99,43	2,52,97
1945-46	3,60,67	2,80,44
1946-47 (R.E.)	3,36,19	2,68,02
1947-48 (R.E.)	1,78,77	1,62,06
1948-49 (B.E.)	2,56,02	2,30,14

The total tax revenue was, for many years, quite inelastic and it was not till 1942-43, that it showed any distinct improvement. While the World War was at its peak, tax was utilized as a very effective and resourceful instrument in expanding the revenues of the Government and this position was not only kept up but the percentage of tax revenue in relation to the aggregate revenue also rose higher and higher. Thus, from 1937-38 to 1942-43, the total tax revenue was in the neighbourhood of 45 to 50%; it suddenly went up in 1944-45, when the War was terminating, to 63%, and in subsequent years it marked 75%, 80% and 90% till in 1948-49, it is estimated that taxation by itself would strengthen the revenue position to the extent of 85%. These figures reveal how taxes provide a flexible machinery which can be geared in such a way as to squeeze from the people as much as the state requires in times of emergency and in periods of dire necessity. Three years after international hostilities ceased, we find that the tax source is being tapped at the rates prevalent

during War-time, although it is recognised that non-tax sources also have been playing an increasingly important role in recent years. Notable among the latter category are Railways, Post and Telegraphs, and Currency and Mint. In 1937-38, nearly Rs. 33 crores have accrued from Railways and Rs. one crore from Post and Telegraphs. This portion of revenue increased by slow degrees till in 1942-43 Railways began to contribute Rs. 74 crores and Post and Telegraphs five crores ; in 1943-44, Rs. 80 crores and 10 crores. But since 1945-46 it showed signs of a sudden decline as Railways yielded Rs. 32 crores, though Post and Telegraphs was still remunerative. From 1946-47, this source of revenue had almost dried up as it brought only Rs. six crores into the public treasury that year, and according to the budget estimates for 1947-48 the contribution from this source is likely to be Rs. $4\frac{1}{2}$ crores. In 1944-45, Currency and Mint yielded Rs. 12 crores and increased to Rs. 16 crores in the two subsequent years. The year 1947-48 witnessed a remarkable dwindling of revenue under this item, though 1948-49 is estimated to contribute nearly Rs. 9 crores. The Indian tax programme, though tended towards appreciable progression during the War, direct taxation continued to be promising even after the War. This does not necessarily mean that direct taxation should be switched in such a way that it mars business incentives and damps enterprises; on the other hand, it can influence production by its effects on the business motives of individuals and can encourage them to enter into new ventures and take new risks.

The fiscal measure of taxation as a whole during recent years has developed a form "incentive taxation", which covers "a variety of proposals providing preferred treatment for income from business enterprise and establishing rewards and penalties considered appropriate

to stimulate output."* But the question may be posed whether tax structure should solely be designed with an eye to provide direct incentive to production. "Taxation is not a means, in our opinion, of supplying a positive stimulus to greater activity. The true incentives lie elsewhere. Taxation can impede their expression in greater or less degree according to the character and the weight of the taxes."† That is exactly the reason why with a view to arriving at the precise character of tax policy and the weight of tax burden, we have bestowed our attention on a brief study of the direct and the indirect facets of the same. Indirect taxation has been generally characterised as regressive and, though it serves as a mighty economic force yielding substantial revenue, its effects will surely be to raise the price of the taxed articles, which mostly will fall under the category of general consumption, and entail hardship on the lower rather than on the upper strata of the society. Economic force of taxation should not only be focussed at obtaining more and more revenue but should also endeavour to "mitigate, not aggravate inequality in the distribution of income."† Thus, indirect taxation would be justifiable only when greater progression of the same through the imposition of heavier rates of "luxury taxation on expensive articles" can be maintained. "In our view, luxurious expenditure should be limited by measures designed to secure a more equal distribution of wealth, and not by selecting particular articles as objects of luxury taxes. Our recommendations, however, in regard to commodity taxation are directed not so much to the imposition of particular taxes primarily for other than revenue purposes as to the use of such taxation as an important instrument of revenue."‡ While dicsussing about

* Harold M. Groves: Production, Jobs and Taxes.

† Tax Programme for a Solvent America, by the Committee on Post-war Tax Policy, 1945

‡ National Debt and Taxation Committee Report (1927)—Minority Report.

taxation as a fiscal measure, we should see that economic justice is not lost sight of. It is one of the vital canons of tax justice that taxes should be direct rather than indirect. Direct taxation as a powerful economic force yielding more substantial revenue than indirect taxation involves a "mere transfer, but no reduction, of aggregate purchasing power", and forms a potent instrument for stimulating or giving incentive to business enterprise. The principles of "progression" and "differentiation" we have referred to earlier have contributed not a little to the economic justice in direct taxation. "The essential ingredients of this economic justice are equality, or uniformity and universality of taxation." * Hence modern economists have been keen to emphasize the economic force of justice in taxation. This is true of almost all the important countries in the world, whereas in India, with the levy of progressive death duties, not only would it contribute mightily to the fiscal armoury of the country, but would also bring about a justifiable distribution of national income.

Taxation as a Social Measure

It is a well-known fact that while the fiscal objective of taxation is to pool up revenue, its other object is to effect some desirable changes in social relations. "This anti-thesis rests upon a failure to observe that finance, like economics is a social science, and that even from the narrow political point of view of the relation between the government and the citizen, the government cannot derive any revenue—that is, cannot take any part of the social income—without inevitably affecting social relations. The fact that the government has in mind solely the fiscal aim of securing revenue does not alter the social consequences of the particular revenue system. In modern times, social conditions are influenced to a large extent by changes in wealth. Every tax necessarily affects the wealth of indivi-

* Seligman: Modern Problems in Taxation.

duals, and if we could in all cases trace the final consequences of even a 'purely fiscal' tax, all kinds of unforeseen results, social as well as fiscal, or perhaps better social than fiscal, would disclose themselves."* Thus, all economic actions do have social effects. All these effects have to be brought to the crucible of justice and all systems of taxation have to be in conformity with this canon. The social object of taxation has been very clearly emphasized in the following words of Kalidas, the National Poet of India: "As the sun draws moisture from the earth, in order to give back in the shape of rains, for fertilizing the land, and producing the sustenance of the people, so the King levies taxes for utilising them for the good of the people." As the state thus began to indentify itself with the welfare of the people, it naturally assumed responsibility of embarking on programmes which seek to aid in the processes of education and medical comforts to impart a sense of social security and to improve the standard of living of the masses by executing reconstruction plans. Public expenditure and taxation have therefore assumed conspicuous roles from what the older school of economists held, and the increase in expenditure has been witnessed among democracies, monarchies and dictatorships, for in all of them the tide of social force has been very swift. The expenditure programme should be so tailored as to suit the social needs of the country as a whole. "The objects of expenditure" said Mr. V. L. Mehta, "for which Government require larger resources are such as subserve the purpose of building up in the Free India of the future an educated, healthy, industrious community—for the furtherance of which objects expenditure has to be incurred by Government rather than by individuals. *They represent an enlargement in the social purpose of the whole community.*" †

* Seligman: Essays in Taxation.
† Mr. V. L. Mehta's Budget Speech on 26 February, 1948.

This brings into bold relief the principle of public versus individual expenditure. Much emphasis has of late been laid on the fact that "a small sum spent collectively on needs which are urgent yields more significant results than a large sum spent indirectly on needs which are not", as Prof. R. H. Tawney has observed, and it is by such "systematic and well-directed diversion of personnel and social expenditure that we can proceed to establish economic equality." The Finance Minister, Bombay, quoted the following words of Prof. R. H. Tawney: "Equality is to be sought not by breaking into fragments the large incomes which are injurious both to those who receive them and to those who do not, but by securing that an increasing proportion of wealth which at present they absorb will be devoted to purposes of common advantage." Thus, we find that all public expenditure can be better utilized for common good than private or individual expenditure and that taxes represent the amount that can be usefully spent "without depriving the common man of the right to spend his income as he chooses," directing thereby all expenditure into socially desirable channels. The social force of taxation can not be appreciated unless the long-range effects of taxation upon the social structure of the society as a result of the uses made by the state of the tax revenue are clearly understood.

This leads us to a study of expenditure in the important countries of the world. Here we are not concerned with the classification of public expenditure. Our aim is only to show how best the state has been endeavouring to utilize taxation as a social measure, remedying, at least partially, the social evils, by regulating the scales of distribution and the equitable utilization of purchasing power, through a systematic public expenditure. Taxation in conjunction with a sound expenditure policy proves highly beneficial, from the social point of view. Social expenditure, which means expenditure incurred with a view to further-

ing social objectives, such as the development of the government industry into a socialistic system, a deliberate re-distribution of the national income, relief to the sick, the invalid, the old and the unemployed and a high level of literacy, has been of a recent origin. This might enter into conflict with production as a whole and to it has been attributed the charge of damaging the industrial economy of a country. That is an unkind and unbecoming charge, and it may be quite pertinent to quote Mr. R. H. Brand, who, while not objecting to social expenditure, in his evidence before the Colwyn Committee, professed himself as "out of sympathy with a great deal of modern thought which regards very large expenditure by the government on social schemes of all kinds as synonymous with progress" and which does not balance "the probable or possible social advantages" against "the certain disadvantages of less saving and less enterprise, leading in their turn to a lower standard of life all round and less employment."

Above, we have presumed that social effects might counteract the progress of industry as a whole, but this argument is untenable as the greatest social advantage and the best interests of production are, however, not so hostile to each other as they might appear. For, as Professor Pigou has remarked: "from a distributional point of view, it would plainly be best to take nearly all your money from the rich people, but that might be so bad from a productive point of view that the poor people would in the end be damaged."* The Finance Minister of a country would therefore naturally prescribe a limit beyond which socially desirable expenditure should not be incurred much to the detriment of the national economy and enterprise. He would always be imbued with he fervour of instrumentalizing this aspect of expenditure as a force for

* Report of Committee on National Debt and Taxation, 1927.

increasing the national economy and its productive resources.

Let us now survey the part that social expenditure plays in the field of public expenditure in different parts of the world.

(a) *India*

Social expenditure in India has not been of an appreciable order, and our country has been most conspicuously lagging behind several others in endeavouring to ameliorate the social condition of our people. Social expenditure comprises expenditure especially on education, public health and other social services which indirectly strengthen the productive power of the people. In 1937-38, expenditure on social services, such as education and public health, stood at 15% of the aggregate expenditure, while in Canada it was 36%, in the Union of South Africa 33%, in Australia 29%, and in the United States 41%. "India has none of the expenditures which have transformed the expenditure structures of some Federations since the greatest depression—expenditures on unemployment relief", says Findlay Shirras.* The meagre amount of money that is being spent for services has been a blot on the part of the financial authorities. In recent times, however, the provinces have been devoting their attention towards expanding the nation-building activities to some extent. The expenditure on these activities includes items like education, medical services, public health, irrigation works, etc. The following table shows the percentages of nation-building expenditure to total expenditure in all the eleven provinces before the partition. †

* Findlay Shirras : Federal Finance in Peace and War.

† Dr. Lanka Sundaram & Vithal Babu : Union Finances.

Percentage of Expenditure on Nation-Building Activities. (*Total Expenditure*= 100)

Province	1944-45	1945-46 R. E.	1946-47 B.E.
Madras	20	22	29
Bombay	16	26	24
Bengal	17	27	22
Punjab	22	23	20
U.P.	28	20	21
Bihar	23	23	20
C.P.	..	17	21
Sind	15	16	19
Assam	21	27	17
Orissa	9	12	14
N.W.F.P.	21	19	13

It will not be possible to distinguish from the above percentages the importance of the different services that constitute nation-building activities. Yet it can be said that there was a phenomenal rise in expenditure on education, while in the case of medical relief and health, the progress is not encouraging.

The part that a well-balanced expenditure programme plays can be gauged from an insight into the report submitted by Mr. Layton, wherein he said :

> "The extent to which taxation is felt as a burden depends very largely on the objects on which a government spends its revenue. Thus, it has been frequently pointed out that taxation for the purpose of paying interest on an internal debt is economically speaking a transfer of wealth within a country, which may—it is true—hamper enterprise if the method of raising the revenue is unwise, but which need not do so or

affect the total saving power of the community. Again, wise expenditure on social services and particularly on health and education should be remunerative in the sense of increasing the wealth-producing power and, therefore, the taxable capacity of a country. Security is, of course, essential, if production is to develop; but it cannot be claimed for expenditure on defence either that it is a mere redistribution of income or that it promotes productive efficiency." *

The passage gives an idea as to how best results a system of social expenditure would produce. Small wonder, that the Government of India, despite the prospective buoyancy of revenue, did not launch upon any remarkable social programme to improve the social condition of the poverty-stricken masses! They neither initiate any welfare programme nor undertake to promote the well-being of the industrial and agricultural workers. It was only in the beginning of 1948 that the State Insurance Bill was passed. There is therefore sufficient scope in India for utilizing taxation as a potent social force.

(b) *United Kingdom*

The following items in the current expenditure account of the United Kingdom show how much is being spent for social services:

EXPENDITURE (in million £)

Heads	1938	1944	1946	1947
Social Security Payments:				
a. Non-contributory pensions	47	110	131	49
b. Family allowances	—	—	19	55
c. Milk and vitamin products	—	21	28	36
d. Unemployment allowances	35	2	4	3

* Indian Statutory Commission (Layton's Report).

EXPENDITURE (*Cont.*)

(in million £)

Heads	1938	1944	1946	1947
Other transfers:	41	98	548	254
Exchequer contributions to national insurance fund:	47	59	60	136
Subsidies:	14	196	314	418
Total	184	486	1104	951
Total current exp.	793	5512	3324	2841

The amount that was spent in 1938 formed nearly 23%; in 1944, 5%; in 1946, 33-1|3%; and in 1947, 33% of the total expenditure. The Central grants to the National Insurance Fund, are being utilized along with the contributions of employees, voluntary and employers' contributions, and investment income for meeting current expenditure on goods and services and some transfers to private current account as the table on the next page would indicate:

National Insurance Fund

(in million £)

	1938	1944	1946	1947		1938	1944	1946	1947
Direct taxes	55	70	86	112	*Current expenses on goods and services*:				
Indirect taxes	54	71	84	116	Medical benefit	12	15	19	21
Incomes from property	9	15	20	21	Expenses of administration	14	11	15	17
Grants from Central Government	47	59	60	136	*Transfers to private current a/c*:				
					Contributory pensions	47	65	75	214
					Sickness benefit	22	32	32	32
					Unemployment benefit	55	4	26	28
					Saving:				
					Surplus on Current account	15	88	83	83
Revenue	165	215	250	395	Current expenses & surplus	165	215	250	395

It will be seen, that the Central Government has contributed £47 million for meeting a total expenditure of £150 million in 1938, £59 million for meeting £137 million in 1944, £60 million for meeting £177 million in 1946 and £136 million for meeting £312 million of current expenditure. This explains only the amount set apart for meeting the several heads of expenditure over and above those mentioned in the table showing the social payments expenditure, subsidies, etc.

A clearer picture has been given about the Public Social Services in the statement given by Mr. Glenvil Hall, the Financial Secretary to the Treasury, on 19, December 1947 as indicated in pages 38 and 39.

(c) *United States of America*

Though the federal expenditure policy was at the outset very conservative and was devoted mainly to fulfilling primary functions, with the New Deal policy and due to the consequent revolutions in the social aspect of life, money incurred with a view to provide social amenities showed an appreciable increase in the United States till if bulked 40.7% of the aggregate expenditure in 1937-37. Before the outbreak of the War, social welfare expenditure which included work relief and direct relief, assistance to the aged and other social groups, promotion of public health, unemployment and accidental compensation, social security administration, etc. figured nearly 70%. But all of a sudden with the impact of the War, more and more expenditure had to be met on defence measures with the result that the total sum spent on social welfare became insignificant. During 1944, only 2% was devoted for social services, as $1,055 million could be utilized out of $95,573 million. With the prevalence of normalcy, the tide turned. While total expenditure lessened, the percentage of social welfare expenditure began to rise. In 1947, it was nearly 5%, ($1,570 million out of

Service	1945-46 (or latest available) year) (1)	1946-47 (estimated) (2)	Total number of persons directly benefitting from expenditure included in Col. (1)	(3)
	£'000	£'000	England and Wales	Scotland
Unemployment Insurance & Unemployment Assistance	20,020	39,350	Over 11¼ million*	Over 1¼ million*
National Health Insurance	57,071†	59,670†	22,131,000*	2,546,000 *
Widows', Orphans & Old Age Contributory Pensions	64,020 ‡	88,799	2,574,387	304,000
Old Age Pensions	58,229	103,552	2,232,000	247,000
Old Age & Widows' Pensions etc., Supplementary Pensions	62,461	39,161	Not available	Not available
War Pensions, etc. (War of 1914-18)	33,949	35,615	593,310	64,890
War Pensions, etc. (War of 1939-45)	48,743	51,429	1,178,540	149,300
Family Allowances	—	33,580¶	—	—
Education	191,136	220,502	Not available	—
Physical Training and Recreation (1937 Act)	3	33	Not available	—
Approved Schools	2,637	2,956	11,052	3,752
Public Health: for Hospitals and Treatment of Disease:	25,561)	Not		
Maternity and Child Welfare Work and Midwives	8,175)	available	Not available	Not available

CONTINUED

Service	For details as per page 38			
Lunacy and Mental Treatment.	10,789	Not available	127,614	23,599
Mental Deficiency				
Relief of the poor	41,658	Not available	540,699	108,417
Housing	55,198	Not available	—	—
Total 1945-46:				
England and Wales	597.126			
Scotland	82,524			
Great Britain	679,650			

* Number of insured persons at 7th July, 1945 (Unemployment) and 31st December, 1946 (Health).

† Calendar Years 1946 and 1947.

‡ Exchequer contribution 1945-46, £22,525,000.

¶ Family Allowances began in August 1946. The numbers of children in respect of whom allowances were in payment at 31st March, 1947 were: England and Wales. 3.569,000; Scotland, 535,000; the number of families concerned being: England and Wales, 2,288,000; Scotland, 306,000.

a total of $12,873 million). According to the estimates of 1948, out of the total expenditure of $37,528 million, $1,654 million was devoted for social purposes, which comes to nearly 5.3%.

It may be recalled that the recent Taft Bill aimed at improving the literacy position of the people of the United States and $300 million have been set apart with a view to equalizing educational opportunities by distributing this sum by way of federal aid to the States. That too has been considered as a small drop in the $6 million bucket which the National Federation Association has aimed at as its target. Expenditure on education is thus bound to act as the opening wedge to better social and economic relations.

(d) *Australia*

Amongst the three main functions of the Commonwealth of Australia upon which expenditure is incurred, social services are a secondary function. Before the War when the tax structure as a whole was regressive, the percentage of expenditure spent on social services to the total was nearly 18. With the outbreak of War, though the tax structure became more and more progressive, the same percentage of the aggregate expenditure could not be devoted for social services, comprising education, public health, invalid and old age pensions, unemployment relief, maternity allowances, etc. On the other hand—naturally too—defence expenditure increased enormously and it stood nearly at 55% of the total expenditure during 1943-44. In 1946-47 also, it was nearly 50%. So much attention could not be focussed on social services during the War and the aggregate amount spent on these services began to dwindle year by year. In 1942-43, only 12% of the expenditure was utilized for social services, in 1943-44, only 11%; and in 1946-47, 15%. The revenue which was being derived from taxes was being utilized for social purposes and to that extent, taxation became an effective social instrument.

(e) *Canada*

In the Dominion of Canada, public welfare receives very great attention of the public authorities and forms a major item of expenditure under the head 'secondary functions'. The place of public welfare expenditure can be clear from the following figures:

Details	(in thousand $) 1939	1943
Public welfare :		
Health & Hospital care ..	47,145	51,856
Labour & Unemployment Insurance ..	3,272	31,458
Relief ..	82,629	6,362
Old age pensions ..	39,587	47,551
Other items ..	35,613	39,725
	208,246	176,952
Education ..	128,682	150,893
Total	336,928	327,845
Total expenditure	1,230,661	5.539,051

The total amount spent for public welfare services and education constitute nearly one-fourth of the total expenditure in 1939, but only one-twentieth of the total expenditure in 1943.

(f) *U.S.S.R.*

The fiscal system of the U.S.S.R. is very interesting in so far as its revenue and expenditure policies are linked up with the lot of the masses and any changes in those fields reflect the interest which the state evinces on matters relating to the collectively estimated social needs. Natur-

ally, therefore, the proportion of expenditure for national economy and welfare and culture services looms large. In 1940, the U.S.S.R. Budget showed for the above heads about 48% of the total expenditure.

With the outbreak of the War, the social and cultural policy could not be pursued with the same force as in pre-war time; and the fiscal system was confronted with the task of providing funds for national defence. All the same even during the War, the expenditure on social welfare and national economy did not fall below 20% of the aggregate expenditure of the U.S.S.R. Notwithstanding the fact that military expenditure takes away half of the State Budget, the estimates for 1944 did provide for a substantial sum for social and cultural services and it represented 38.2% of the total budget.

The share of expenditures for national economy and culture, as given out in the State Budget of the U.S.S.R. for 1948 by the Deputy A. G. Zvenev, Minister of Finance, was estimated to increase to 68.4% as against 66.2% in 1947, and the share of expenditure for the defence was reduced to 17.0% as against 18.4% of the previous year. Expenditure on Defence seems to be very meagre. But the survey on the Soviet Budget in the "Economist" of February 14, 1948 says:—

> "It is difficult to compare the proportion allocated to defence in the Russian and other budgets, because of the vast differences between the structure of those budgets. The expenditure of the governments, for instance, does not include such massive appropriations for national economy as does the Russian Budget. If the figures of the Russian Budget were to be re-arranged so as to be comparable with the budgets of capitalist countries, it would probably appear that the Soviet outlay on defence amounts to 25-30 per cent., and not to 17 per cent. as claimed, of strictly governmental expenditure. This gives a measure of the drain of the 'cold war' on Russian economic resources."

Regarding expenditure on social services, the surveyor observes:

> "The second biggest item in expenditure, coming next to the national economy and before defence is, however, 'social service.' Of the 116 million roubles allocated for that purpose, nearly 60 million roubles is for education. In addition to that, about 30 million roubles are spent on education for the budgets of the republican and provincial administrations. Thus, the total national expenditure on schools is still nearly 50 per cent. higher than the expenditure on defence or than capital investment in the basic industries. This year 33 million pupils receive education at Soviet Schools—722,000 at the universities and high technical schools. The 'cultural revolution' in Russia is still in full swing."

Thus even taking for granted the argument that "the expenditure of other governments, for instance, does not include such massive appropriations for national economy as does the Russian Budget",* the point will be more clear and complete that the expenditure met by the U.S.S.R. Government is very much substantial and that very few governments in the world can establish even half of its record in the matter of social services.

Summary

The paragraphs on 'Democracy and Economy' and 'Government and Economy' serve by way of introduction to the study of taxation as a fiscal and social measure. The statistics that have been presented in the two paragraphs dealing with 'Taxation as a Fiscal Measure' and 'Taxation as a Social Measure,' disclose the position that not only the revenue side can be substantially increased by having more direct taxes, but also that the expenditure on social services has been ignored in India, and to that extent the state is in default in this country.

* 'Soviet Budget Survey,' The Economist, Feb. 14, 1948.

CHAPTER 2

REDISTRIBUTION OF WEALTH

1. INEQUALITIES OF INCOMES FROM INBORN GIFTS AND ENVIRONMENT—2. INEQUALITY OF INCOMES FROM WORK—3. INEQUALITY OF INCOMES FROM PROPERTY—4. THEORIES OF DISTRIBUTION AND DISTRIBUTIVE JUSTICE—5. NATIONAL INCOME AND EXISTING INEQUALITIES—6. REDISTRIBUTION OF WEALTH—7. SUMMARY.

> "The drift of economic science during many generations has been, with increasing force, towards the belief that there is no real necessity, and therefore no moral justification, for extreme poverty side by side with great wealth."
> —MARSHALL.

In the previous Chapter, we observed that absolute equality was a pre-requisite of economic democracy. This does not lead us to observe that perfect democracy needs must insist upon equal economic welfare, because of physical, mental and economic differences amongst the people, which can be substantially related to their individual merits. Even under conditions of absolute economic democracy, it is rather doubtful whether equality of opportunity in all walks of life can be guaranteed to everyone. Equality of opportunity is a difficult ideal. This concept merely means an equal chance to all become unequal. * Admitting the basic equality of men in a court of law, the more gifted persons have to be better rewarded, as otherwise society as a whole will grow static. As long as personal differences exist along with privileges, there are bound to be disparities in individual achievements and in economic rewards. The myriad personal differences that exist today are responsible to some extent for the inequality that abounds in any society. Several democratic ways and means are being pursued for lessen-

* S. Howard Patterson ,A. W. Setroyen Little & Henry Reed Bourch: American Economic Principles, 1941, p. 379.

ing the adverse effects of these differences by a continuous process of the three R's—Relief, Recovery and Reform—as in the case of the New Deal Programme in the United States. Thus, the bridging up of the wide gulf of capacities and abilities between different individuals is an impossibility. Economic democracy can only throw open a window in the pursuit of economic equality by bringing about a redistribution of the wealth of a society on an equal basis, so that the present economic contrasts may not be as grave and severe.

It is common knowledge that extreme poverty exists side by side with abundant wealth and that, within the frontiers of a small country itself, such economic maladjustments and dis-equilibrium, are the iron facts of today. This contrast between poverty, on the one hand, and plenty, on the other, based upon the size of incomes, leads us to a study of several causes for the prevalance of inequality.

Inequality of Incomes from Inborn Gifts and Environment

There is a very wide-spread misconception about the causes of economic inequality in general. Inequality, according to some, is a direct result of unequal abilities and endowments amongst men. Canon Temple, in his Economic Sermons to the students of Repton School affirmed that "if you take a large number of people, with varying abilities, but not very varying selfishness, and put them to live together for several generations, the result will be the accumulation of wealth in comparatively few hands." * Varying abilities necessarily mean varying productive powers and, as the productive power increases or decreases, the returns for the same will naturally be quite different. As long as incomes are dependent ultimately on the productive powers of different men who participate in production so long the returns from work

* Repton School Sermons, pp. 171-172.

are bound to vary in individual cases. Differences in ability may be due to natural or inborn differences owing to gifts which are ultimately responsible for the inborn superiority of some over others. "Inequalities of position and possession arose from the inborn superiority of some men over others."* In our present day economic activities, it is quite apparent that those born with a silver spoon in their mouth begin their life with rather definitely greater prerogatives, while those born poor are faced with an infinite variety of impediments and deficiencies. That is exactly the reason why it is rightly believed that "the rich are growing richer while the poor poorer."

It is often believed that while inborn inequalities that are being transmitted from one generation to another are solely responsible for the unequal economic circumstances, the past that environment and opportunity play in lessening, to some extent, the disadvantages with which those persons begin their life, should not be forgotten. Some differences in remuneration and in consequent social stratification are of course due to inborn superiorities, and great talents are rewarded substantially as exceptional abilities obtain exceptional returns. "The analogies of heredity suggest that the qualities of such ancestors were transmitted to their descendants and that the so-called higher classes of modern times constitute a born aristocracy. Though heredity is irregular in its individual manifestations, for large numbers it shows regularity and persistence. Take a thousand children of gifted parents and a thousand children of mediocre parents; the former will prove the superior class, even though a sporadic genius may emerge among the latter. Can it not be inferred that the broad differences between social classes rest on differences in their inherent inherent intellect and moral endowments?"†

With the development of the social structure of society, such inborn differences are not allowed to be perpetuated or established firmly. This is not tantamount

* F. W. Taussig Principles of Economics, Vol. I, p. 297.
† F. W. Taussig: Principles of Economics, Vol. II, p. 232.

to a complete disappearance of those undue advantages enjoyed by some at the cost of society as a whole. But it shows signs of a serious breakdown in that scheme of things with the advent of a powerful influence of "environment". The word 'environment' should be understood in a comprehensive sense to include "all causes of unequal opportunities to obtain income except the inheritance of property." * Enviromental differences do exist and they provide almost insuperable barriers and only those persons with a very high order of ability can escape the influence of enviroment. Position, prestige and possession of any individual can be co-related to the surrounding enviroment and the opportunities within the reach of that individual bring about variations in talent. On the other hand, different enviroments conduce to different occupations, whether skilled or unskilled. In the case of the former, a long and expensive technical training may be necessary. But for the initial expenditure that is involved before a person enters into a specialized industry which requires a highly technical skill, everybody would have tried to enter that occupation. Naturally, in specialized industries the level of wages would also be high in contrast to that of the unskilled which do not insist upon so much of technical training. Thus, several trades and occupations are barricaded by high costs of training and education, with the result that the ultimate number of workers in such a specialized industry would be rather small. As the demand for these workers would be relatively great, they naturally would get better wages. Those persons who could reap the benefits of a costly training emerge as a different class altogether, while others unable to do so fall into a different class. Owing to lack of equal opportunities for training and education, differences arise in the incomes of men. The management of large-scale business insists on a peculiar knack of grasping things and taking decisions in time and the most successful entrepreneur always has those native talents. Persons well-versed in the theoretical aspect

* Dalton : The Inequality of Incomes.

of business undertakings, might prove unsuccessful in the practical field. The fact that some time unskilled labourers do obtain higher wages, only proves that differences in native ability and in technical training result in inequality of incomes from work. Moreover, climatic conditions which vary so much from place to place might require only a type of skilled labour for the industrial undertakings in a particular locality and, if a higher grade of talent is available and if there is no free movement of labour it would not obtain the most deserving wages in relation to productivity. Even, on the other hand, if a lower grade of talent is available, it will not well suit industry as a whole. It is therefore possible to find economic inequality not only in different occupations but also in one and the same locality, with the result that extreme poverty exists side by side with great wealth due to inborn abilities, enviroment and opportunity.

Inequality of Incomes from Work

Inequality of incomes from work depends upon, according to Dalton, the amount and the value per unit of work performed. "The inequality of incomes from work depends partly upon differences in the amount of work performed by different individuals and partly upon differences in the value of different kinds of work." * Taking the first cause of inequality of incomes, it can be said that differences in the amount of work performed by different individuals depend upon not only the ability of the individuals, the training they obtain in their respective occupations but also the various legal prohibitions that might be imposed with a view to restricting entry into certain occupations. To add to this, workers in the same occupation performing varying amounts of work also receive different wages. On the other hand, different occupations employing different kinds of skilled and unskilled men cause unequal incomes from work. Coming to the second cause of inequality of incomes from work,

* Dalton: The Inequality of Incomes, p. 252.

the value of any piece of work depends upon the law of demand and supply—the relative demand for different commodities and services and the relative supply due to several elements like the "general nature of the work, its agreeableness or disagreeableness, the social esteem in which it is held, the prospects which it is thought to offer of exceptional success, or security of employment, and its supposed chances of sickness or accident." If all occupations were to afford the same attraction to all wage-earners, there would never be different incomes from work. Not only because of the changing advantages or disadvantages in the different occupations but also of the varying degrees of skilled and unskilled labour that is at present available, inequality of incomes from work becomes a more potent cause.

Inequality of Incomes from Property

Inequality of incomes from property is very significant under modern economic conditions than that of incomes from inborn gifts and environment and from work. Dalton summarises the three immediate causes of inequality of individual incomes from private property as follows:—

> "First, differences in the amounts of property received by different individuals by way of inheritance and gift, second, differences in the amounts of property accumulated by different individuals by way of saving, and third, the changes which take place, apart from the action of the respective property owners, in the value, both capital and annual value of different pieces of property" *

Saving: Let us analyse the two minor causes of inequality before we enter into a discussion of the wider question of inheritance. Saving is a potent way of accumulating incomes in the form of property with the express intention that it would not only form a fiscal reservoir in the lean years of life, but that it would also contribute to the status and the position of the owner. Saving is not

* Dalton: The Inequality of Incomes. p. 272.

within the reach of all individuals and depends upon the aggregate income-surplus, which an individual has in excess of the amount of expenditure involved in providing for himself and his family the bare necessities of life and some comfort. It will be difficult to arrive at an agreement as to the amount of money which an individual can save, without undergoing any sacrifice of economic welfare. Saving also depends to some extent, upon the property the individual previously possessed, for, otherwise his present income might not enable him to save continuously and substantially. It is a well known fact that the rich can save more than the poor. While the former enjoy an economic surplus, the latter groan under an economic deficit. The rich following an uninterrupted scheme of saving become richer, while the poor unable to meet even their day-to-day obligations become poorer. It is therefore obvious that, while on the one hand the aggregate amount of money saved increases, inequality, on the other, must be disproportionately increasing. It is an accepted principle that "saving does not mitigate inequality arising from other causes but aggravates it."* This is not to be blind to the several advantages that accrue from large-scale savings which ultimately bring about an appreciable expansion of industrialization.

Value of Property: Under modern conditions a constant change is taking place in the incomes from different pieces of property without any reference to the individual actions of the property owners. These differences may relate to those "in the value, both capital and annual." Due to the external influence, it is quite possible that persons may "grow rich in their sleep," as it were. For instance, during the boom days of the Second War several businessmen, speculators, contractors and land owners got rich quick, and a compradore class was set up. All this occured without any proportionate effort on the part of the recipients of larger incomes due to sudden demand

* Cannon: Wealth, p. 186.

for their services and goods. Prices ran high and rewards were relatively great. Despite steep taxation, businessmen, either by black-marketing or by a system of speculating, enriched themselves. There is also a counterpart to this. In a period of economic collapse or crisis, prices might considerably fall down and any deliberate policy of inflation might not restore the price structure to its former level, with the effect that the economic machinery as a whole might be dislocated. The persistence of economic mal-adjustments might bring about utter dis-equilibrium and reduce the richer members of society to poverty. These cyclical changes are likely to prove beneficial or baneful, as they bring in their wake perceptible changes in the economic relations of different strata of society. Inequality has, therefore, every reason to substantiate its ground under those circumstances. Without any corresponding increase or decrease of productive power, economic rewards of different individuals may fluctuate due to some external influences. Unequal incomes that aggravate inequality make it difficult to be avoided.

More important is the direct cause of inheritance of property. Property is the ownership of wealth and comprises such objects as land, buildings, machinery and personal mortgages.* Inequality of incomes from property in any society depends upon the relative scope of public and private property.† It is a truism that the more the scope for private property, the greater the degree of inequality arising from incomes from property, and the more the scope for public property the less the degree of inequality.

Private Property: In a primitive society private ownership consisted largely of land. Land which was held under common ownership became private property, either due to the breaking up of the family unit, or because of reforms in the order of cultivation. Later on, ownership included all the personal belongings, and the owner had the freedom

* Buehler: Public Finance, p. 400.

† Dalton: The Inequality of Incomes, p. 276.

to possession, use and dispossession of the same. The rights attached to private property are quite significant. The term 'right' can be looked at from two points of view. * Firstly, an individual might have manufactured certain things in the sense that he has put in his labour and so given an attribute of value-in-use to that particular product. Secondly, an individual might also be carried away by the presumption that he could utilize the product for his own personal requirements. Even under primitive conditions, such rights of private property were subject to certain limitations—limitations under the heads of origin and use. In fact the product with which the individual "mixes" his exertion of body or mind is itself limited in quantity; so also with the utilization of any natural resource that contributes in the production of national income. But if private property is justified and rationalized by its contributions to personalty, two conditions result. Firstly, every person has a legitimate right to acquire property, and any social economic order that fails to obtain this primary right to him will defeat the purpose for which it stands. The right to the acquisition of any property is not limited to a chosen few. Secondly, nobody should be allowed to possess so much of property that may be effectively utilized against the interests of the economy of the society.

The word 'property' under modern conditions has become more and more significant, and the possession of property means a fountain of power, prestige and position. Almost all castes, political and social, have crumbled before the citadel of property. As J. A. Hobson says: "In the earlier stages of acquiring property, the solid advantages of material security and comfort compete with the zest of successful struggle; but established men of property tend to value their wealth more for the social consideration it brings and the visible satisfaction of seeing other persons bend to their will." † At the present day,

* Hobson: Wealth and Life, p. 142.
† Ibid. p. 150.

political and economic democracy has been evidently combating with private property. Political equality has come to clash with the present scheme of private property. Though it is quite apparent that in most advanced countries of the West, the organized unions of labour could not show much ability or capacity to utilize to the full their fervour against the propertied men, the U.S.S.R. has shown the possiblity of a different order altogether. The socialist ownership of property constitutes the economic foundation of the Soviet society, and it means that all the major industrial establishments, and all the implements and means of production belong to the society, co-operative enterprises or public organizations, but not to individuals.* The private property which comprises money, bank notes, securities, personal furniture, agricultural implements etc., can be owned by individuals, though they are forbidden to own land, forests, mineral deposits or means of production that can be exploited only with the aid of hired labour. Article 10 of the Soviet Constitution (1936) guarantees the right to a certain amount of personal property and of restricted inheritance. It reads thus: "The right of the citizen to personal property in their income from work and in their savings, in their dwelling houses and auxiliary husbandry, in household articles and utensils, and in objects of personal use and comfort, as well as the right of inheritance of personal property of citizens, are protected by law." In the U.S.S.R. too, private property of the a citizen is protected by law, though limitations are imposed in respect of the kind of property that individuals are entitled to own.

Inheritance: "The inequalities of property which arise from unequal industry, frugality, perseverance, talents, and to a certain extent even opportunities are inseparable from the principle of private property."† Private property provides the substance for inheritance. Inheritance does

* In the Land of Socialism, p. 263.

† Mill: Principles of Political Economy.

not represent wealth which is a fruit of labour but consists of that personal property which is transmitted at death of an individual to be inherited by his legal heirs under his will or by the exercise of legal right. The right of inheritance, has been restricted in several countries and differences exist in their respective laws of inheritance. Whatever the laws of inheritance, it can be affiirmed that a majority of men and women leave their property to their dependents and relatives. A man or a woman has however the freedom in most of the countries to leave the property to whomsoever he or she chooses.

Inheritance is an indispensable part of the institution of property and its economic effects on the equality of incomes are very grave. In innumerable instances the right to inherit was not conceded, with the result that, after the death of individual proprietors and landowners, all their possessions, had to be transferred to some organization which acted as a trustee.* But this is not a common occurrence.

Historically speaking, the possession of property was largely responsible for the commonness of the family unit and its devolution to the surviving members meant "no change of ownership but a transfer to new representatives of the continuing owners" †—a transfer that gave full freedom to the inheritors to do what they please with the property.

Proper attention is not bestowed on this aspect of inheritance. "For half a century and more, the rights and responsibilities of living men may be determined by an instrument which was of no effect, until the author of it was in his grave and had no longer any concern with the world or its affairs. The power of the dead hand is so familiar a feature in our law, that we accept it as a matter of course, and have some difficulty in realising what a very singular phenomenon it really is." ‡ But

* Wedgewood: The Economics of Inheritance, p. 51.
† Taussig: Principles of Economics, Vol. II, p. 299.
‡ Salmand : Jurisprudence, p. 422.

there can be no doubt that the inherited property enlarges unequal status creating unequal economic opportunities and expanding individual incomes disproportionately. The inheritors start life better and command all amenities—medical, physical, educational, etc., thereby ultimately bringing about an appreciable increase in their standard of living. Biologically also, it has been proved that men with greater means have shown less aptitude for a number of children, while the poor who have none from whom they can inherit substantial property, have always a very big family. The greater the proportion which the inherited property bears, the greater will be the inequalities of incomes arising from it. It can, therefore, be said that the most important cause of inequality of incomes from property is the fact that some persons inherit much larger property than others, with the result that incomes from work also vary as the inheritors possess more and more economic opportunities. Thus, inherited property will bring about more capital and "he who controls capital controls the economic life of a country. The influence of the master of capital extends beyond individuals and classes; it reaches to the state, to the society as an organised whole. The master of capital possesses an immense power to impose his will upon the state, implied in his power to withhold help when it is urgently needed or to damage the economic machinery of the country. In a very important sense the mastery of a country's capital is the mastery of that country." * Inheritance thus gives its owner the power to control the economic machinery of the country which in turn promotes social stratification.

The institution of inheritance has threatened democracy by the concentration of private economic power in the hands of a few people. "Our society," according to Irving Fisher, "will always remain an unstable and

* Manchester Guardian, 23 May 1918.

explosive compound as long as political power is vested in the masses and economic power in the classes. In the end, one of these powers will rule. Either plutocracy will buy up the democracy, or the democracy will vote away the plutocracy." * Such a danger had been foreseen by President Roosevelt in his message on 29 April, 1938 and he cited official figures to prove that, of the inherited property, 33% was concentrated in only 4% of all the estates reporting to the Government. Emphasising the same fact, Dr. Cannan wrote: "Every one knows that in all cases except the newest countries, teh inequality in the amounts of property which individuals have received by way of bequest and inheritance is by far the most potent cause of inequality in the actual distribution of property." †

The importance of inheritance as a serious factor, resulting in maldistribution of property, has been underlined by Taussig: "the influence of inheritance is enormous..... Obviously this alone explains the great continuing gulf between the have's and the havenot's." The influence of inheritance on the distribution of property works directly on the total wealth, and also indirectly on the amount of savings. Though the income from property is less than that from work, the former is much more unequally divided than the latter, and to that extent is wholly responsible for the mysteries of inequality in the distribution of national income.

Theories of Distribution and Distributive Justice

The mastery of economy, under capitalism, lies in the hands of the capitalist who commandeers the means of production into any channel he chooses. He is only imbued with the thirst for a greater and greater profit, and the low wages with which he engages labour mark the

* Irving Fisher: Economists in Public Service, American Economic View, March 1919.

† Cannan: The Division of Income, Quarterly Journal of Economics, May 1905, (reprinted in the Economic Outlook, 1912,)

injustice of the system of distribution. Ruthless exploitation of the surplus-value of the wage-earning classes is the order of capitalism and capitalistic countries do betray a steep gradation of incomes. 'Rugged individualism' exists under the cover of capitalism, and the individual capitalists while trying to enrich themselves, leave the workers impoverished. This has been much substantiated in the inter-war period when businessmen, industrialists, speculators had amassed unparalleled wealth, while any doubling or trebling of the wage rates could not cope up with the soaring price level.

Capitalism has prepared the basis for socialism; it has yielded place to a new and more scientific social order, in which profit motive disappears. There is social production for social appropriation. "Socialism requires that the processes of production and distribution should be regulated, not by competition with self-interest for its moving principle but by society as a whole, for the good of society. * Economic machinery has therefore, to be geared consciously in the best interests of society as a whole.

Considering on such a broad basis, some individual liberties are likely to be curtailed and no one would be allowed to take out of the pool of wealth of the society more than one's share. While ensuring some equitable distribution of national income, socialists permit differences in income based on differences in economic contribution.† However, they would avoid completely or restrict sharply property income in the shape of rent on land and interest on capital. With the socialization of property and the elimination of profits, inequality due to vagaries in unearned incomes, will not be visible on a substantial scale. Earned incomes in the form of remunerations, like wages and salaries which loom large under a socialistic scheme, will, no doubt, contribute to some differences among

* Palgrave: Dictionary of Political Economy, "Socialism."
† S. Howard Patterson, (A W. Selwyen Little & Henry Reed Bourch): American Economic Principles, 1941, p. 379.

the recipients of income. But these differences exist and continue to exist as long as individual peculiarities abound. They will not lead to great variations in the individual incomes, as all incomes would be received by those who have rendered services and no income would accrue from wealth or property owned. Socialistic distribution is always guided by considerations of collectively estimated social good, with the result that only a few differences, which cannot be otherwise eliminated, would prevail.

Under Communism, guided by the Saint Simonian maxim "from each according to his powers to each according to his needs," a different interpretation is given to the distributive theory of income. It is feared that the maxim in practice, would eliminate the incentive for greater production and the productive effort would very soon show signs of discouragement. The primary urge which drives men to mental and physical exertions would be conspicuously lacking in as much as the possibility for increasing profit seems to have been sapped. The reward for individual skill, initiative, daring and perserverance seems under Communism to be meagre and human effort would be reduced to a common unproductive level. Yet, it cannot be denied that Communism would imply a conscious desire for the good of the community which appears to be far stronger than self-interest. The philosophy of Saint Simon and his followers was admirably epitomized in a brochure first published in 1830:

> "They reject the system of community of goods, for this would be a manifest violation of the first of all the moral laws which it is their mission to teach—viz., that in the future each one should rank according to his capacity and be rewarded according to his works.
>
> "But in virtue of this law they demand the abolition of all privileges of birth, without exception, and consequently the destruction of inheritance, the chief of these privileges, which today comprehends all the others, and the effect of which is to leave to chance

the distribution of social privileges among a small number, and to condemn the most numerous class to privations, to ignorance, to misery.

"They demand that land, capital, and all the instruments of labour should become common property, to be so managed that each one's portion should correspond to his capacity, to his reward to his labours."

The theory of distribution under communism would naturally eliminate remarkable variations in so far as the principle of common property would not leave any room for windfalls, leaving sufficient scope for economic equality to prevail as national wealth would be held in common and national income would be distributed among all members of the community in relation to their respective needs.

This leads us to a study of distributive justice. The two main principles, according to Dr. Dalton, in economic justice, are: first, "distribution according to deserts," and second, "distribution according to needs." There are three interpretations of distribution "according to deserts."* First, the absolute equality of incomes; second, distribution according to the value of work done, provided equality of opportunity is obtained; and third, distribution according to the value of work done in the existing state of society.

Absolute equality of incomes is highly improbable and even if an attempt were made to achieve it, it would hamstring economic initiative and decrease economic welfare. The second interpretation i.e. 'distribution according to the value of work done after having obtained equality of opportunity' is another impracticable principle. The concept of equality of opportunity means "an equal chance to all to become unequal." It is fair to say that equality of opportunity is the first essential of justice in the body politic and economic. It is equally chimerical

* Dalton: The Inequality of Incomes, p. 20.

to say that absolute equality of opportunity cannot at all be conceived of.

The third interpretation, i.e. 'distribution according to the value of work done in the present state of society,' depends upon the entirely unequal opportunities of work, that is to say, those variable strictly from the income point of view. As a social order which drives out unequal opportunities is an impossibility: so also is distribution according to the value of work done. But all these interpretations do not leave us cold to think that equality of incomes from work is purely Utopian.

The next principle of "distribution according to needs," is explained by Dr. Dalton: "The meaning of 'needs' is not altogether clear, but if we understand by an individual's needs his capacity for making good use of income, this doctrine is identical in practical effect with the principle suggested for securing an ideal distribution from the point of view of economic welfare, provided that its application does not react unfavourably upon production and other relevant factors." * Distribution according to needs does not sound sense, for the needs of the people vary so much owing to differences in climate, the status of the individual, the number of dependents, etc., and it would be futile to think about justice from this point of view. No society has been uptil now founded on such distributive justice.

Under capitalism, distributive justice has no meaning, for it is the capitalist who determines what justice, or often injustice, should be meted out to his wage-earners. Under Communism and Socialism, distributive justice connotes equal opportunities for work and equal incomes from work according to the Saint Simonian principle mentioned above.

National Income and Existing Inequalities

The concept of 'national income' is a new addition to the family of statistical instruments and vocabulary.

* Dalton: The Inequality of Incomes, pp. 24-5.

National income or dividend comprises "the labour and capital of the country acting on its natural resources," which "produces annually a certain net aggregate of commodities, material and immaterial, including services of all kinds." * It is the result of co-operation of all these various productive agents, land, labour, capital and organization of various kinds. The problem of distribution of national income has been engaging the earnest attention of all countries.

(a) *India*

Several estimates have been made from time to time of the national income of India. The first estimate was on the basis of figures relating to years 1860 and 1870 by Dadabhai Naoroji, who estimated the national income of British India to be £340 million which came to 40 shillings or Rs. 20 a year per head. In 1882 Earl Cromer and Sir David Barbour estimated it to be nearly Rs. 525 crores which came to Rs. 27 per head per year. For the year 1898-99 Willian Digby estimated it to be Rs. 428 crores which meant Rs. 17½ per head per year. Lord Curzon, on the basis of the Report of the Famine Commission of 1898, came to the conclusion that the average income was Rs. 30 per head in 1900 against Rs. 27 in 1880. Shah and Khambatta calculated the total average income to be Rs. 1,106 crores per year from 1900-1914, and Rs. 1,862 crores from 1914-1922. This meant a *per-capita* income of Rs. 37 per year from 1900-14 and Rs. 58½ per year from 1914-22. Findlay Shirras has put the *per capita* national income to be Rs. 107. Dr. V. K. R. V. Rao's calculation of national income for 1931-32 ran between Rs. 15,878 and Rs. 17,904 million. According to him, the same thing can be put in another way by saying that the income of British India for 1931-32 amounted to Rs. 16,881 million with a margin of error of plus 6%, i.e. the *per capita* income amounted to Rs. 62 with a margin

* Marshall : Principles of Economic, 5th Edition, p. 524.

of error of plus 6%. Proceeding on the same basis of the total of urban and rural incomes, unofficial income calculations for 1938-39 and 1942-43 show that the total income of British India for 1938-39 was estimated at Rs. 18,649 million, while in 1942-43 it was of Rs. 42,650 million. According to Sir Shanmukham Chetty, the national income of India after partition was nearly Rs. 4,500 crores in 1947-48. The following figures will show how the national income has been distributed:

Details	1931–32 Dr. Rao's estimate.	Estimates* 1938–39	Estimates* 1942–43.	Estimate 1947–48
Total rural income (Rs. million.)	12,250	11,631	23,797	25,000
Rural population (in millions.)	228	249	261	260
Per capita per annum income (Rs.)	51	47	91	96
Total urban income (Rs. million.)	4,928	7,018	18,853	20,000
Urban population in millions)	28	35	39	40
Per capita per annum income (Rs.)	166	200	483	500
Total income (Rs. million)	17,178	18,649	42,650	45,000
Total population (millions.)	256	284	300	300
Ratio of rural to urban population.	8:1	7:1	20:3	19:3
Total per capita per annum income (Rs.)	65	66	142	150

Considerable progress seems to have been made in the national income which is more than double in 1947-48 as compared with that in 1938-39. The *per capita* figures do not reflect the precise position of the general progress and prosperity of the country. The figures for years during and after the War might mislead us to think that as the *per capita* income had risen the general fiscal position was more solvent and sound. The defect in all these calculations is that they cannot record the distribu-

* India's National Income, Commerce, 18th December, 1943.

tional side of national income. It is most probable that a very small proportion of population might be possessing a very large percentage of national income, of which in the end, the bulk of the population might have at its disposal, a meagre part. Though an increase in the aggregate national income can, other things being equal, suffice to show that there is every possibility for the *per capita* income to increase, there is no proof of its equitable distribution. The only possible way to ascertain the present trends of equality, or to be more precise inequality, in the distribution of incomes, is by presenting a picture of the range of incomes and the number of house-holds:

Number of Households		Incomes
		Rs.
6,000	Over	1,00,000 a year each
270,000	Averaging	5,000 ,,
250,000	,,	1,000 ,,
3,50,00,000	,,	200 ,,
Remainder.	,,	50 ,,

These figures are quoted in the "Times Trade and Engineering Indian Supplement" of April, 1939, under the caption, "The Indian Market." These figures of income do not show that income was distributed inequitably before the War of 1939-45. To have a more precise view of things, we take below the income returns of 1937-38:

Families.	Range of Income.
About 701,000	Over Rs. 1,000 a year.
,, 263,000	Between 1,000 to 2,500. a year
,, 148,000	,, 1,500 to 2,000 ,,
,, 104,000	,, 2,000 to 3,000 ,,
,, 79,000	,, 3,000 to 5,000 ,,
,, 58,000	,, 5,000 to 10,000 ,,
Less than 10,000	,, 10,000 to 12,500 ,,
About 17,000	,, 12,500 to 25,000 ,,
,, 5,300	,, 25,000 to 100,000 ,,
,, 352	,, 100,000 to and over ,,

While that was the position in the pre-war time, the following table shows the number of income-tax assessees for the year ending 31st March 1947:

Range of Incomes			Assessees
Rs. 2,000	to	5,000	2,39,647
5,001	to	10,000	1,00,990
10,001	to	15,000	33,749
15,001	to	25,000	23,730
25,001	to	1,00,000	17,900
Above Rs. 1,00,000			2,985

It is quite clear now that inequality that existed before the war has been aggravated due to conditions of wartime. On the distribution of national income in India, Jathar and Beri observe:

> "The learned professions and the bigger land-owners enjoy a very much higher income than the cultivators or industrial labourers. The petty traders and shopkeepers have incomes of a medium size. Among the urban classes probably half of the total income belongs to one-tenth of the people. Among those with incomes exceeding Rs. 2,000 a year, 38% have only 17% of the total income, while about 1% possess 10% of the total income. The inequality of distribution is equally evident among the agricultural classes and is indicated, among other things by the distribution of agricultural holdings. For instance, in Bombay, out of 22 lakhs of registered holders of land, 10 lakhs have each a holding below 5 acres in size, i.e. 48% of the land holders possess only 9% of the cultivated land, while 1% of the land holders possess 16% of the total land, the results of the large classes of the landless agricultural labourers whose economic position is definitely lower than that of the holders of land.
>
> "The result of this calculation is that more than a third of the wealth of the country is enjoyed by about 1% of the population, or, allowing for the

dependents, about 5% at the most; that slightly more than another third, about 35% of the annual wealth produced in the country, is absorbed by another third of population, allowing for dependents; while 60% of the people of British India enjoy among them about 30% of the total wealth produced in the country."

These estimates show that poverty has been on a steady decline, and also that distribution is not at all even. National income has increased and along with it the per capita income too; urban prosperity is achieved by increasing rural poverty.

Sir Shanmukham Chetty as the Finance Minister, in one of his public utterances, referring to the middle classes as the sheet-anchor of the Government's fiscal programmes, said that the middle class people could be defined as those whose annual income falls between Rs. 3,000 and 10,000 i.e. those with incomes varying from Rs. 250 to Rs. 850 per month. It is doubtful whether those whose income exceeds Rs. 500 per month, could be included in middle class. Even strictly conforming to the Finance Minister's viewpoint, nearly 320,600 assessees are paying tax on incomes between Rs. 3,000 and Rs. 10,000 annually, and those with incomes of Rs. 10,001 and above are nearly 78,364. In other words one-fifth of the total assessees are responsible for nearly half of the total income assessed while less than half the total income assessed, is collected from nearly four-fifths of the total assessees. The range of inequality that exists at present is quite apparent. (Income-tax returns for the year ending 31st March, 1947).

United Kingdom

In United Kingdom, the national income has increased since 1938 as:

Year	National Income
1938	About £ 4,707 million
1942	„ 6,000 „
1944	„ 8,600 „
1946	„ 8,100 „
1947	„ 8,770 „
1948 (estimated)	„ 9,000 „

While in other countries, the national income has more than doubled, in Great Britain it could not be so because of the excessive hardships during the war. These figures however do not show how economic power is concentrated in particular classes. Some facts about the income distribution in the United Kingdom in 1938 were brought together in the White Paper issued by the Chancellor of Exchequer (1944). Out of private incomes (excluding undistributed profit and including transfer incomes), nearly 4% accrued to 8,000 income-receivers with more than £10,000 a year each; or (if each of these income-receivers maintains 4 persons) to nearby one-tenth of 1% of the population; about 12% to 1,05,000 income-receivers with more than £2,000 a year, representing some 1% of the population; one fourth to 8,00,000 income-receivers with more than £500 a year, representing 7% of the population. The following figures show the position in regard to the distribution of incomes just before and after the War.

Distribution of Private Income by Ranges of Income

Range of Income-Tax	No. of Incomes	Total Income before tax	Total Income after Income-tax and tax at.		Proportion of income before tax retained after deducation of taxes at.	
			1938-39, rates	1946-47. rates	1938-39. rates	1946-47 rates
		(000)	£ millon		per Cent	
Private income in 1938						
Private income at the disposal of individuals which can be allocated to different ranges:						
Under £250	...	2,463	2,459	2,443	99.8	99.2
£250-500	2,000	679	662	625	97.5	92.0
£500-1,000	670	455	415	360	91.2	79.1
£1,000-200	224	304	259	209	85.2	68.8
£2,000-10,000	98	360	255	185	70.8	51.4
£10,000- and over	8	175	76	36	43.4	20.6
Private In. come in 1946						
Private income at the disposal of individuals which can be allocated to different ranges.						
Under £250	...	3,030	3,023	2,996	99.8	98.9
£250-500	6,600	2,260	2,207	2,086	97.7	98.3
£500-10,000	1,740	1,190	1,093	951	91.8	79.9
£1,000-2-000	495	670	578	466	86.3	69.6
£2,000-10,000	157	547	392	293	71.7	53.6
£10,000- and over	8	148	68	35	45.9	23.6

The number of persons paying income tax was 3,000,000 before the war increased to 9,000,000 by the end of 1946. On a closer observation it will be seen that while those income receivers upto £1,000 who bulked 89% in 1938 had a total income of 72%, only 11% of the tax payers had 28% of total; while those income receivers upto £1,000 who bulked 89% in 1946 had a total income of about 66-2|3% while the remaining 11% of the income tax payers of the upper brackets had 23-1|3% of the aggregate income. These figures crystallize that though the number of income tax payers trebled and though the aggregate income tax doubled, inequality of incomes has not increased remarkably.

United States of America

The national income of the United States of America has considerably increased:—

Year	Total national income in billion
1939	70.8
1942	122.2
1944	160.7
1945	161.0

Along with the mounting national income, concentration of economic power in the hands of a few has also been evident. The analysis of the distribution of income in the United States of America in 1935-36, prepared by the National Resources Committee, revealed that of 29,400,300 families in the U.S.A.

Over 4 million families, or more than 14% of the total, had incomes less than $500.

About 12½ million families, or more than 41% of the total, had incomes less than $1,000.

About 19 million families, or more than 64% of the total, had incomes less than $1,500.

Over 25 million families, or 87% of the total, had incomes less than $2,500.

Only about 1 million families, or 2.8% of the total, had incomes in excess of $5,000.

About 270,000 families, or 0.97% of the total, had incomes in excess of $10,000.

Recent studies of the tax structure of the United States of America show that in 1939, just before the War, families and single individuals in the lowest income group who had an average income of about $346, paid 22% of their income in hidden taxes and consumers' levies. Although the families and single individuals having incomes of $20,000 or more paid 37.8% of their income in taxes, no amount of reasonable progression was pursued in the tax burdens of the different income groups. The highest income classes averaging $47,600 a year and comprising only 0.3% of all income classes, enjoyed 8.4% of the total income having set aside 30.4% of all positive savings made by the American people even though this class paid 17% of all taxes.

President Harry Truman in his economic report submitted to the Congress in January 1948 said: "Not only did average incomes increase....., but also important changes occurred in income distribution. The relative increase in income (before taxes) was greatest for families in the lower-and-middle-income groups. For example, the increase in incomes between 1941 and 1946 was over 60 per cent. for the lowest 40 per cent. of families and only 20 per cent. for the highest 20 per cent. of families." This can be seen from the following table:

Average Family Income

Families grouped from lowest to highest income	Money Income before Taxes; 1946 dollars			Percentage increase	
	1935-36	1941	1946	1935-36 to 1945	1941-46
Lowest fifth	$ 446	498	835	87	68
Second fifth	969	1,275	2,023	109	59
Third fifth	1,515	2,243	3,050	101	36
Fourth fifth	2,284	3,225	4,201	84	30
Highest	5,928	7,412	8,921	50	20
Average for all families	2,229	2,932	3,806	71	30

No explanation is needed here. The lowest 40 per cent. of families had an increase of over 60 per cent. of their incomes and this formed a slice of the tax revenue naturally.

In 1946, many families had incomes below what can be considered adequate standard. 28 per cent. of the families had money incomes less than $2,000 and 48% less than $3,000 as shown in the following table:

Percentage Distribution of Families by Income Levels in 1946

Civilian money Income classes (1946 dollars)	Percentage of families	Cumulated percentage of families
Under 1,000	12.8	12.8
1,000 to 1,999	15.4	28.2
2,000 to 2,999	19.5	47.7
3,000 to 3,999	18.4	66.1
4,000 to 4,999	13.0	79.1
5,000 to 7,499	13.0	92.1
7,500 and over	7.9	100.0

Consideration of the civilian money income classes up to $2,000 shows that nearly 28 per cent. of families came into this category. Thus, with incomes between $2000 and $5,000, there are 50% of the families. Coming to the latest income distribution for 1947, the following figures reveal the number of families with two or more individuals and the number of families comprising single individuals;—

Income distribution for the year 1947

Income Class	Families of two or more				Single Individuals			
	*Number		Cash Income		Number		Cash Income	
	Percent	Million	Percent	Million	Percent	Million	Percent	Million
Total	100	35.4	100	116.7	100	12.5	100.0	18.3
Under $500	6.8	2.4	0.8	0.9	23.6	2.9	6.2	1 1
100-1,000	12 1	4.3	2.8	3.3	28 2	3.5	13.4	2 5
1,000-1,500	12.6	4.5	5.7	6.7	18 2	2.3	17.7	8.2
5,500-2,000	13.2	4.7	7.7	9.0	12.7	1.6	16.2	3.0
2,000-3,000	24.4	8.6	20.5	23.9	10.0	1.3	17.7	3.2
3,000-5,000	20.9	7.4	27.2	31.7	5.5	0.7	16.9	3.1
5,000 or over	10.0	3.5	35.3	41.2	1.8	0.2	11.9	2.2

* As actually published in Family Income and Post-war Markets, these percentages were adjusted slightly and rounded to the nearest one per cent.

Canada

The National income at factor cost is increased in Canada since 1938:—

Year	Net National income in $ million
1938	3,940
1939	4,221
1944	9,685
1945	9,627

Net national income at factor cost measures the net value of production and variations in this total from year to year indicate the economic position of the country as a whole.

The net national income expanded from $3,940 million in 1938 to $9,685 million in 1944 and dropped slightly to $9,627 million in 1945. If we take details that comprise the net national income, it will be clear that in 1938 salaries, wages and supplementary labour income were nearly 62% of national income at factor cost, while investment income represented 18% and net income of individual enterprises 20%. The proportions in 1945 were: Salaries, wages and supplementary labour incomes amounted to 52%; Military pay and allowances to 11%; investment income to 19%; net income of individual enterprises to 18%.

The above figures indicate the distribution of the net national income at factor cost during the four years mentioned above; it will be interesting to investigate as to what percentage of the income class groups are responsible for what percentage of the total national income.

Estimated number of tax-payers, total income and tax collected by income classes, 1945

Income Classes		Tax Payers (No.)	Total Income $000	Total Tax $000
Below 1,000	dollars	425,300	349,621	18,271
1,000 to 2,000	,,	1,252,000	1,877,938	139,712
2,000 to 3,000	,,	478,200	1,128,916	131,884
3,000 to 5,000	,,	144,000	526,071	97,876
5,000 to 10,000	,,	48,500	324,369	92,455
10,000 to 25,000	,,	14,200	204,519	87,557
Over 25,000	,,	2,800	131,477	86,741
		2,365,000	4,542,911	654,496

The income class group up to $2,000 which comprises 71% of the total tax-payers is responsible for 24% of the total tax revenue, having a total income of 49% of the whole. Those with incomes between $2,000 to $5,000 who bulk 22% of the total numbers of tax payers, contribute nearly 33% of the total revenue with a total income of 25%. The remaining 7% of the tax-payers with incomes over $5,000 are responsible for nearly 35% of the total tax revenue with a total income of 25%. The following figures show the details of the income classes.

Estimated number of tax-payers and total income in 1945

Class		Tax Payers (Number)	Total Income $000	Total Tax $000
Single, No. dependants	...	903,890	1,225,182	219,162
Single, one or more Dependants	...	66,880	102,126	13,648
Married No. dependants	...	543,355	1,240,668	202,821
Married, one dependant	...	390,835	884,647	111,989
Married, two dependants	...	269,240	612,967	63,461
Married, three dependants	...	128,455	295,327	26,068
Married, four dependants	...	44,085	118,162	10,799
Married, five dependants	...	12,845	41,561	4,009
Married, six dependants	...	5,415	22,271	2,539
	Total ...	2,365,000	4,542,911	654,496

AUSTRALIA

Australia which belongs to the high income groups shows these details:

Year	National income (£ A. million)
1938-39	803
1939-40	852
1942-43	1,229
1944-45	1,228
1945-46	1,236
1946-47	1,265

The table shows the effects of the changeover from a peace-time to a war-time economy from the angle of national income. There has been a steady increase in the national income upto 1941-42 and it was followed by an increase of nearly 25% till 1946-47. Its steadiness was not a little due to the fact that the Australian economy had been much dependent on international trade. The distribution of income shows how different tax payers enjoying different incomes, pay the income-tax:

Grade of Taxable Income

Assessment year	£200 and under	£201 to 500	£501 to 1,000	Over £1000	Total
1938-39					
No. of tax payers	199,482	69,454	38,303	27,525	334,764
Tax assessed	£225,744	414,564	779,325	5,839,145	7,258,778
% of total tax	2.0	3.0	6.7	50.8	63.1
1939-40					
No. of tax payers	214,341	71,033	37,108	26,092	348,574
Tax assessed	£261,661	466,344	842,157	5,852,654	7,422,816
% of total tax	1.7	3.0	5.5	37.8	48.0
1942-43					
No. of tax payers	202,510	1,096,668	149,422	47,878	1,496,478
Tax assessed	998,515	2,055,290	14,668,404	42,504,616	83,226,825
% of total tax	0.7	18.6	10.9	31.8	61.8
1944-45					
No. of tax payers	493,155	1,249,567	243,225	66,906	2,052,853
Tax assessed	1,341,938	14,727,845	8,970,648	15,886,210	40,826,641
% of total tax	1.3	15.4	9.3	16.6	42.6
1945-46					
No. of tax payers	505,955	1,251,392	224,393	59,323	2,041,063
Tax assessed	£5,135,719	57,759,134	33,602,948	52,215,432	148,713,233
% of total tax	2.5	27.8	16.1	25.2	71.7

It is clear that in the Commonwealth of Australia, on the eve of the Second World War, 60% of the total tax payers with incomes of £200 and under contributed to the public treasury only 2% of the aggregate revenue, while nearly 8% of the total tax payers paid 50.8% of the aggregate revenue, enjoying incomes over £1,000. During the peak year of the War (1942-43), the distribution of incomes must have changed remarkably, as is shown by the figures. Persons with incomes of £200 and under were exempted from income tax to a great extent with the result that though the tax payers were nearly 13% of the total number, they paid a very negligible percentage of 0.7, while those with incomes ranging from £201 to £500, who bulked 73% contributed to the Exchequer 18.6% of the total revenue. Those with incomes over £1,000, who were one-third of the total, contributed 31.6% of the total revenue. The figures of the latter years show a decidedly better change.

U.S.S.R.

The concept for 'national income' in U.S.S.R. has a limited meaning as national production embraces only material production, i.e., the outputs of agriculture, industry, building construction, and the services of freight transportation and of retail trade.* This meaning has been often attributed to Marx, but some Soviet economists like Chernomordik and Strumlin are of opinion that Marx never intended to confine the scope of national production to the creation of physical goods only, and that "all labour resulting in the creation of surplus value and capital formation, and that he (Marx) specifically disclaimed the validity of the distinction of productive from unproductive labour by the mere form of the created product" according to Paul Studenski and Julius Wyler. It has been advocated that the Marxian meaning to national production and national income "in terms of the operations of the capitalist society and might, have been modified and broadened considerably if made in terms of the operations of a socialist order."

* In the Land of Socialism.

According to prices in 1926-27 the national income has increased from 25 billion roubles in 1928 to 125 billion roubles in 1940, national income has risen by 400%. Thus within a period of twelve years, national income has risen by 400%. Paul Studenski and Julius Wyler observe after a careful study that the last breakdown of national income in constant prices by different sectors of production was in 1937. "It shows," they argue, "increase in their income for the nine-year period of 1928-37 ranging from 66% for agriculture to 264% for retail trade, 400% for transport, and 485% for industry." This high record was registered because of the fact that producers' goods were manufactured on a large scale than the consumers' goods.

Thanks to the socialization of production, no exploitation of man by man in the U.S.S.R. has been witnessed. According to the census of 1939, industrial workers constituted 32.3% of the working population, collective farmers 44.6% and office employees, etc. 17.5%. Thus, the Soviet society which consists of the working class and the peasantry, formed the social classes without any instinct of exploitation of one by another. Both of them jointly wield power. Workers are always imbued with the fervour that the more they produce the more they receive in the shape of national income and the more prosperous the whole of the community is likely to be. This gives rise to "mass labour heroism." "It inspires the millions of Soviet men and women to put their best into their work." The socialization policy and the part that labour plays along with the peasants, prove that equality, to a very great extent, is bound to exist in the socio-economical structure of U.S.S.R.

Redistribution of Wealth

So far many figures have proved that wealth is unequally distributed. There is an expression, "Optimum Distribution" of wealth. As Jensen wrote: "If regard is had solely to the consumption of the national income, at a given moment, an optimum distribution would be one yielding the maximum aggregate satisfaction, which

would clearly not be an equal distribution. For the needs, or the capacities for enjoying wealth in the spending, are not equal, varying with age, health, sex, education, and so on." An optimum distribution of wealth is one, under which the marginal rupee, pound or spent dollar would yield equal satisfaction to all. While aiming at an optimum distribution, one should be careful to bear in mind a long range view of its effects "with respect to their disposition to save and with respect to their efficiency in employing capital created by saving." Redistribution of wealth attempted by the public authority, should be cautious enough to aim at an optimum distribution, thereby lessening the rigours of inequality.

The important instruments utilized for redistribution of wealth are taxation, public expenditure and borrowing.

Taxation as an Instrument for Redistribution

Taxation is being utilized as a legitimate implement for redistribution of wealth in a country. A form of income redistribution is in vogue with the advent of the levy of income tax which takes away a portion of the aggregate income received by individuals, lessening inequalities in the distribution of wealth or to be more precise, to redistribute wealth on an equitable basis by a system of progressive taxation. Progressive taxation means that the larger the income, the steeper the rate of taxation imposed. The exemptions that embody income-taxation make it easier for redistribution of wealth, with the result that the poor are left untaxed and that the rich are taxed at progressive rates. The effect will be that the aggregate tax revenue would be spent upon public social services, etc., to ameliorate the condition of the have-nots. To the extent that income tax from the wealthier classes is utilized as a perennial stream to finance poor relief, medical aid, education, unemployment relief, and a host of others, which aid the lower income groups, it can be said that distribution of wealth has been adjusted. On the other

* Jens. P. Jensen: Government Finance, p. 219.

hand, if taxes are regressive, that is to say, if the rates of the taxes decrease as the income increases, it would aggravate inequality.

Death duties are being levied for bringing about the most desirable distribution of wealth. Jensen said: "Death taxes are most effective in equalizing wealth. To be most effective in its equalizing function, the tax ought not only to be progressive according to the size of the estate, in case of an estate tax, or progressive according to the size of each share, in case of a tax on the separate shares, but also progressive according to the amount of wealth possessed by the legatee. Perhaps income taxes may also be made steeply progressive on the total income; and taken together with steeply progressive death taxes, would be effective equalizers. General property taxes, where general property means the net worth of the tax payer, might be, but have seldom been effective equalizers." *

President Roosevelt in his message to the Congress on 19 June, 1935 referred to the existing concentration of wealth and pointed out that the ill-effects of such concentration could be reduced by heavier inheritance taxation, while at the same time some much needed tax revenue could be procured. Death has been taken as a very opportune occasion in the re-distribution of incomes from property, and a more equitable distribution of wealth could prevail by employing a system of death duties; so also in the case of gifts which take away a major slice of the wealth of the deceased the tax could be utilized for the benefit of the society.

In addition, there are taxes which are not progressive or whose progressivity is limited, as in the case of the corporate incomes. "A tax on corporate incomes would sooner or later reduce dividends; but the reduction would be proportional to the dividends received not progressive on the wealth of the stockholder. Even so, since a larger proportion of large incomes than of small incomes is

* Jens. P. Jensen: Government Finance, pp. 219-20.

derived from dividends, some equalizing would result." * Redistribution of wealth can best be done with the help of progressive direct taxes. To that extent, taxation is a safe implement for equalizing the wealth of all.

Public Expenditure

Public expenditure in conjunction with the revenues derived to cover it can operate sufficiently well in lessening or increasing the inequalities of the income of the individual members of society or allowing the present system of distribution to remain unregulated. "While new expenditures have been met by various revenues, tax systems have commonly placed relatively heavier burdens on the lower incomes than on the higher and have thus, to some extent, offset the effects of the expenditures. In recent years in the United States, however, the highly graduated federal income and estate taxes have apparently had the effect of causing the ratios of total taxes to incomes to increase among the classes paying these taxes."† Study of social expenditures in important countries reveals to what extent a scheme of public expenditure can be utilized as an influential instrument for either redistribution of wealth, or for lessening the inequality of incomes from work as from property.

When a loan is raised and is utilized to finance any expensive scheme of public works, it might be drawn from the higher income groups. To that extent, the total income of society is redistributed, bearing in our mind the direct and indirect effects of the same. It is also probable that inequality in the distribution of wealth might be increased when the upper income classes who should pay progressively higher rates of taxes are furnished a means of avoiding those taxes by purchasing tax-exempt securities. That is why such securities are not in the interests of an equitable redistribution of the wealth of society.

* Jens. P. Jensen: Government Finance, p. 220.

† Buehler: Public Finance, p. 184.

If borrowing is undertaken from the rich for the benefit of the masses, it means that if the rich are asked to finance some socially-desired-expenditure schemes, inequality in the distribution of wealth can be lessened; it also means that a redistribution of income can be conceived.

Redistribution of incomes can be attempted in three ways though the success cannot be guaranteed. In this book, a study of redistribution of incomes from inherited property, is attempted.

CHAPTER 3

History of Death Duties

Death Duties in ancient and medieval times —*a.* India—*b.* United Kingdom—*c.* United States of America—*d.* Australia—*e.* Canada—*f.* *U.S.S.R.*— *g.* France—*h.* Italy—*i.* Germany—Summary.

Death Taxes in Ancient and Medieval Times

One of the oldest recorded taxes that is known to us is the Inheritance Tax. It is regarded generally as a refinement on the estate tax. The tax on property devolving on death can be traced all the way back to early antiquity. The inheritance tax which fell upon the succession of personal as well as of real property can be dated from B.C. 117. Roman authorities in fiscal history have emphasised that the 'Lex Voconia' of B.C. 169 had developed a form of inheritance tax, due to the frantic efforts of Emperor Augustus. Primarily, it assumed the form of a compulsory bequest; later, it emerged into a true inheritance tax, the 'vicesima heriditatium.' In Rome it was at first a 20th of the estate, which under Emperor Caracalla was doubled.* The unmarried were taxed cent per cent, while the couples without any issues paid 50 per cent. The story runs that when for the first time Augustus proposed inheritance tax, the Senate was hostile to the act, but when the Emperor pointed out that the Great Julius Ceaser was in favour of this act all opposition died down. That was how the tax originated in Egypt. The 'vicesima heriditatium' was unlike the former taxes, neither an estate duty nor a probate fee, but was a succession duty, pure and simple, devolving on the actual benefit accruing to the legatee or successor. This was a 50% duty on inheritances and bequests and was levied only with a view to raising funds

* Groves: Financing Government, p. 12.

for pensions and bonuses for the army. In the first instance, it applied only to citizens residing in Rome but was afterwards extended gradually so as to apply ultimately to all citizens who by 212 A.D. meant all the free inhabitants of Europe. The tax was based on the shares received by the heirs, some of whom were exempted fully, owing to blood-relationship to the deceased.

In the middle ages, the Inheritance Tax figured in the form of 'relief' paid to a feudal ruler to take title to a property. Under the feudal system, the right to property was regarded as resting with the sovereign and inheritance could only take place at his sufferance. Bastable maintained that inheritance taxes originated from the feudal practices of early rulers in claiming property, having no owners and from the dues payable to the lords by the new tenants when the previous tenants died.* That means, the estate was allowed usually to pass freely from father to his son; in the absence of direct heirs to the deceased, the property escheated to the Crown, though the relatives could succeed to it if they paid 'relief.' This 'relief' was the feudal equivalent of the modern inheritance tax. Quite distinct from this feudal due, in Germany, Scandinavia and parts of France, there existed in their system a variation of the feudal due known as 'Erbkauf' which meant that it was not the heir who purchased his title from the feudal lord but the vassal who had no children and desired his possession to pass on to a specific relative, the vassal having been assured the transfer of his property, by a payment before his death, to the feudal lord.† It was legally binding on the inheritor to claim the estate within a year, in the absence of which the estate passed on to the feudal lord. But the real enthusiasm for introducing death duties in Europe was roused by the severe economic pressure of the Napoleanic wars. In their desperate quest for the sinews of war, the chancellors turned their wistful eyes on property passing at death as an untapped but promising source of supply.

* Bastable: Public Finance (1903), p. 591.
† Shultz: The Taxation of Inheritance, p. 8.

By about the end of the 14th century, a number of Italian cities propelled by 'vicesima heriditatium' and influenced by the financial exigencies, levied inheritance taxes of one form or another. The struggle in Spain compelled a number of Dutch provinces to institute inheritance tax in the beginning of the 17th century. By the end of the 17th century England, France, Spain and Portugal, with well stabilised national monarchies, had developed modified inheritance taxes. In England, where the feudal exactions of 'relief' and 'prima seisina' fell into disuse, a stamp duty on the probates of wills and letters of administration issued by ecclesiastical courts was imposed by the Stamp Act of 1694.

In France, a registration fee or 'insinuation' was introduced in 1539 and later it was extended so as to include all testamentary dispositions. * In the beginning of the 18th century, Louis XIV made all transference of immovables either between the living or the dead, except those in the direct line, subject to a registration fee and an additional percentage of the tax.

Spain had the ancient feudal exactions which became royal taxes by the 18th century, and they remained a most important form of the levy of inheritance taxes till a registration or transfer tax was imposed in 1792.

A form of registration tax existed in Portugal which, later on, took the shape of inheritance levy. These taxes and levies in ancient and medieval times mark the starting point of the introduction of death duties, having been popularised by great exponents like Bentham, Mill and Bluntschile.

Almost all the European countries adopted inheritance taxation during the nineteenth century with a view to provide greater revenue for meeting governmental expenditure and also perhaps for the growth of democratic fervour.

* Pannetier, Les Successions et le fisc (Paris, 1919), Chapter I.

We attempt below a brief historical study of death duties and its various components in the most important countries of the world.

a. India

Though a true form of death duties does not exist at the present day in India, duties on inheritance are, by no means, unknown in this country. Under the Zamorins of Calicut, a duty was imposed on the value of the estates of Muhammedan landlords. * In one of the major states in India, in Bikaner, a form of death duty is levied at the present day, graduated according to the degree of relationship of the legatee or successor to the testator or predecessor. The Government of India considered for the first time in 1859 the imposition of such a tax in their discussions relating to the imposition of income-tax; the financial exigencies after the 'Mutiny' gave an incentive for elaborate discussions on this point. In 1866, Massey pitched upon a scheme of provincial finance in a circular letter addressed to all provincial governments, proposing to transfer to them some heads of expenditure like education, police, public works etc., and hinted that funds might be found from sources like license tax, house tax, octroi and a succession duty. But as the proposal was coldly received by the provincial governments, the Government of Bombay had suggested that the proceeds of income-tax should be distributed amongst the provinces. In fact, the White Paper suggested that the revenue from commercial stamps, succession duties, taxes on railway fares, terminal taxes etc, might fall into the category of those previously under the provincial heads. Indian fiscal system being what it has been—conservative—duties leviable on certain communities have been in force from a very early period.

The principle of death duties was emphasized by the Taxation Enquiry Committee (1924-25). In 1938, a Conference of Finance Ministers was held at New Delhi which urged for bringing the measure into operation early.

* Maclean: Standing information regarding the official administration of the Madras Presidency, p. 84.

The Governments of Bombay, Central Provinces and Bihar suggested that the levy of death duties might be postponed until the national government was formed at the centre, while other governments, like Bengal and the Punjab were much doubtful about the advisability of the measure on ground that their yield might not be substantial because of the implications involved in imposing them. No definite stand was taken by the Governments of Madras and the United Provinces. As such, the issue was shelved for the time being. That very year, the central government circularised the provincial governments for their views on the proposed levy of succession duties. Most of them expressed their disapproval on the following grounds: firstly, the valuation of goods and chattels was difficult; secondly, the habit of investment was still in its infancy; thirdly, there were no precise estimates of trading incomes on which the capital value of business enterprises could be fixed; fourthly, the law of Mitakshara joint family entailed complications too difficult to be surmounted; fifthly, the succession duties could not be levied pending the formation of a popular and national government at the centre and lastly, the succession duty was a communist measure.

There have, however, been small duties levied under the Court Fees Act (1870) on probates, letters of administration, succession certificates, etc. which to some extent, have the nature of death duties in other countries. Prior to 1910, they were levied at a flat rate of 2% in respect of probates, etc., relating to properties exceeding in value of Rs. 1,000, but by the Act VII of 1910, the principle of graduation was introduced in the rates. The maximum rate that has since been raised in Bengal, Bihar, Orissa and Assam was nearly 5%, and was also raised to 7% in provinces like Bombay. Despite the fact that these duties were very much limited in their scope due to differences in race, religion or locality, a considerable amount has been derived from them. These duties have been inequitable in their incidence. The position regarding these

probates was clearly summed up in the Report of the Indian Taxation Enquiry Committee, 1924-25, as follows: "The assets in India of Europeans, Anglo-Indians, Armenians, Jews and persons of foreign domicile must pay duty whether there is a will or not, or whether any right is sought to be established in court or not. The estates of Parsis, whether there is a will or not, and the estates of Indian Christians, where there is a will, must pay duty wherever the estate be situated in India, though only when a right is sought to be established in the courts. The estates of Hindus, where there is a will made in, or relating to, immovable property situated in the lower provinces of Bengal or the cities of Bombay or Madras, must also pay duty, but again only when a right is sought to be established in the courts. The estates of all Muhammadans who die testate or intestate, and the estates of all Hindus and Indian Christians who die intestate and the estates of all Hindus who die leaving will not falling within the scope of the Hindu Wills Act need pay no duty unless the parties themselves apply for and obtain probate or letters of administration." *

The Law of Probate Duties which affords a very complicated picture can be summarised as follows:

Under Section 9 of the Administrator General's Act, 1913, the Administrator General is required to take necessary proceedings to obtain letters of administration in every case in which a person not falling into the category of an exempted † person under the Act dies, leaving within his jurisdiction assets exceeding Rs. 1,000 in value, if no person entitled to the grant of probates or letters of administration has applied for them. The effect of this provision is that the beneficiaries of all Europeans, Eurasians, Armenians, Jews or any other persons of foreign domicile who die testate or intestate, leaving within the

* The Taxation Enquiry Committee Report, p. 268.

† Exempted persons under the Act are Indian Christians, Hindus, Muhammadans, Parsis, Budhists or persons exempted by special order of the Governor General-in-Council under Section 332 of the Indian Succession Act, 1865, from the operation of that Act.

jurisdiction of any Administrator General, assets exceeding Rs. 1,000 in value must obtain probate or letters of administration. Sections 187 and 190 of the Indian Succession Act, 1865, make it compulsory for probate or letters of administration only in cases where rights are sought to be enforced in courts. While this is the position in regard to foreigners dying testate or intestate, Muhammadans, Hindus and Buddhists are exempted from the operation of Section 332 of the Indian Succession Act. The Native Christian Administration of Estate Act VII of 1901 has exempted Indian Christians from Section 119 with the effect that in the case of Parsis letters of administration are necessary or compulsory both in the case of testate and intestate succession, while Indian Christians have to obtain letters of administration only in the case of testate succession. Under the Hindu Wills Act, 1879 (Section 2), the Section 187 of the Indian Succession Act to Wills and codicils made by Hindus, Jains, Sikhs or Buddhists on or after the first day of September 1870, within the territories of the lower provinces of Bengal, or the local limits of the ordinary civil jurisdiction of the High Courts at Madras and Bombay, and to such wills and codicils as though made outside the above years, relating to immovable property constituted therein, was extended. Except in the above-mentioned cases, unless claims are established in a court of law, there is no provision inducing probate or letters of administration either for Hindus or Muhammadans testate or intestate.

Over and above the provisions mentioned earlier, certain laws such as the Government Savings Bank Act 1873, the Post Office Cash Certificates Act 1917, the Provident Funds Act 1897, the Imperial Bank of India Act, 1920, the Indian Companies Act 1913, and the Indian Securities Act 1920, enforced representation indirectly as they embodied certain provisions under which the production of probate or letters of administration can be insisted upon as a condition precedent to the payment of money or transfer of arrears to the successors of the deceased. The Succession Certificates Act 1889 also

embodied provisions facilitating the question of duties on succession and affording protection to parties paying duties to the representatives of the deceased, insisting on the production of a probate, or letters of administration, or a Succession Certificate under the Act. But the duties levied in the Bombay Presidency under the Bombay Regulation VIII of 1827, though levied in the form of court fees, bear to some extent the resemblance to death duties of other countries.

b. United Kingdom

In Great Britain the Inheritance Tax appeared in its embryo as early as 1694 when a Stamp Tax of 5 sh. was imposed on probates over £20. This rate was continued till 1779, when three scales of duty were introduced. By 1889, the duty stood at 3% on all probates and letters of administration. Exemption was also granted to small estates of below £100 and £300. On several occasions, Inheritance Tax projects were introduced in the Parliament but thanks to the majority of the Tory landlords, most of them could not succeed. The strong advocacy of Adam Smith in his 'Wealth of Nations' influenced Lord North who ultimately decided on the feasibility of proportioning the probate duties nearly to the amount of the estate involved.* In 1780 a legacy duty was first levied on the transference of the personal property which was imposed as a tax on the succeeding beneficiaries. Later on, the Probate Duty Act of 1815 imposed a reduction on legacies and bequests where the total estate of the decedent was less than £100. These probate and legacy duties have not undergone any radical change for several years. Meanwhile, there was a great deal of heartburning amongst the commercial and industrial classes about the landed exemption and the progressive rates.† This agitation bore fruit in 1853. Gladstone introduced and successfully enacted his Succession Duty Act that year

* Sydney Buxton and George S. Barnes, A Handbook to the death Duties, p. 5.

† Shultz: The Taxation of Inheritance.

but there has been a good deal of complexity about the levy of the legacy and the succession duties. As Bastable says: "The separation of real and personal property and the favourable treatment given to the former, appeased at first sight a gross injustice. Plausible reasons and especially the alleged heavy local taxation of land might be put forward in mitigation but the striking fact of inequality remained untouched. Settled personality also and with less justification, escaped its proper share of the death duties, with the natural result of encouraging the tying-up of property, and thereby producing economic and financial loss. There was, too, an unnecessary amount of complication in the number of duties and the minute distinctions drawn as to the different interests in property." * Instead of the probate or account duty, which was applicable in cases only of unsettled personal property, the Finance Act, 1894, imposed an Estate Duty on "all property, real or personal, settled or not settled, which passes on the death of such a person" at the graduated rates. This simplifies the whole issue by removing all the previous exemptions and by reducing the number of levies. The duty was to be paid "on any property passing on the death of the deceased" and the valuation in respect of real and personal property on the same basis would naturally bring about desirable changes. The further Estate duty (called Settlement Estate duty) on the principal value of the settled property contributed its might to swell the aggregate revenue.

Thus the complex form of inheritance taxes was codified into a simple law, providing for an estate tax on the net value of real and transferred property, a succession tax on the shares of real property received through property settlements and a legacy duty on the shares of personal property received by the successors of the estate. Later amendments to this Act of 1894 did not bring about any material alterations in the underlying principle but only introduced several changes in the rates of the estate duty and the combined legacy and succession duty.

* C. J. Bastable: Public Finance, p. 598.

The Finance Act of 1914 later provided for a "quick succession discourt" where land or a business or any interest thereon became liable to estate duty. The estate duty increased very slowly, having exempted any estate of the value of £100 and below. A duty of 20% was imposed on estates with principal value of over £1,000,000. A further change in the death duties was brought about in 1919 when the duty reached 40% on estates over £2,000,000, and it meant the extension in 1921 of the exemption on the estates of those dying as a result of active service to cover estates of individuals dying in the Irish disturbances. In 1930, it went up to 50%, in April 1939 to 55%, in September 1939 to 60% and in July 1940 to 65%. The most important change in recent years was witnessed in 1946 when the exemption limit was raised from £100 to £2,000. Thus the small estates on which the rate imposed was very small were exempted as the revenue that they brought in was insignificant. On medium-sized estates, the rates had been made less burdensome, while on the larger estates the rates became highly progressive. Thus the 1% duty on £2,000 gradually rose to 6% on £10,000, 12% on £20,000, 24% on £50,000, 35% on £100,000, 50% on £250,000, 70% on £1,000,000 and 75% on £2,000,000.

(*c*) United States of America

The history of death taxation in America is essentially the history of estate death taxes. According to the tenth amendment, the powers neither delegated to the United States by the Constitution nor prohibited by it to the States have been reserved to the States. The States were far earlier in the field of death taxation and where the Federal Government entered, it did so at least till the close of the 18th century under the pretext of a national emergency and even then only for its duration, repealing the taxes promptly after the period of crisis has been crossed.

The story of the State Death Taxes on inheritance may be narrated under two broad periods—the period upto the end of the 19th century and the subsequent period. The first marked the period when the power of the State to levy death taxes went unquestioned, while the second was pre-occupied with one continuous struggle on the part of the States to resist the encroaching influence of the Federal Authority.

In 1687 provision was made in the Colony of Virginia that its Governor should compulsorily collect as fee a cask of two hundred pounds of tobacco for impressing probates and letters of administration. * Pennsylvania, the earliest of the American States to enter the field, introduced an inheritance tax in 1826. Within 39 years from the inception of the American Constitution (1787), before the Civil War, six more States had followed suit. In 1885, New York came up with a piece of legislation which for its drafting was a model. It imposed a 5% levy on real as well as personal property passing to the successors and applied to such property of non-resident decadents. By 1891, the nine States were administering death taxes. All of them began taxing only collateral heirs at flat rates varying from 2½% to 5% on the estates transmitted. The period 1902-1916 witnessed a stormy upheaval against concentration of wealth. This movement, cheek by jowl with mounting expenditure, threw the whole country into convulsions for additional revenue and new taxes. Death tax became a general favourite and forty of the States plumbed in for death taxation leaving some comparatively less important States—Florida, Mississippi, New Mexico, South Carolina and Alabama—outside the field. This period witnessed the development of the inheritance tax not only in its hold over the States but also in its own interior structure. Much in contrast with the position in 1891 when there were nine States taxing only collaterals at flat rates varying from 2½% to 5% was that towards the end of 1917 when 31 out

* Shultz: American Public Finance, p. 471.

of the 43 States widened the scope of the tax to cover direct heirs and 28 States introduced the refinement of progression with an average rate ranging between 1% to 3% on direct heirs and 5% to 11% on collaterals.

Then followed the second period when the Centre began seriously to compete with the States in the field of death taxation. The Federal Government wanted a share in these taxes during the periods of 1797 to 1802, 1862 to 1870, and 1898 to 1902, and the plea was conceded only in the face of a grave emergency that entailed extraordinary national expenditure. The Federal Government had not the courage to ask for any sort of accommodation in this field during years of peace.

The agitation during 1892-1916 against the rapid accumulation and concentration of wealth in a few hands gave a handle to Theodore Roosevelt in 1906 to recommend to the Congress the desirability of the imposition by the Federal Government of a progressive inheritance tax. The move was stemmed by the opposition combining the conservatives who disliked any extension of death taxes, and those who feared diminuition of State revenues from this tax. There was also the indomitable National Tax Association to be contended against—the Association which had unequivocally expressed its opinion that "inheritance taxes" should be reserved wholly for the use of the several States. This opposition proved effective for some time but when in 1916 the Congress was faced by a 'preparedness' programme, it was swept away, leaving the Federal death tax to have its unquestioned sway.

The end of the World War I left America, however, in great surpluses and everywhere there were proposals to reduce public burden by an overhauling in the field of taxation. The opportunity was readily seized by the opponents of the Federal Estate Tax, and a movement was launched for a total federal withdrawal from the field of death taxes. A curious political alignment was witnessed then in the Congress: the Democrats, though in a minority, never failed to receive the unstinted support of

the indomitable Republicans, either in the House or in the Senate, with the effect that several attempts of the Coolidge administration in the matter of reduction of taxation were frustrated and the same treatment was meted out to the estate tax also. Despite the most fiery condemnation of this tax by the President as well as by Mr. Mellon, the Congress without the slightest perturbation raised the rates and provided credit against the Federal Estate Tax. Unfortunately for the States however, certain things attracted public notice just at that juncture which brought into question the authority of States to continue with the administration of death taxation. Florida had never a tax of this nature, and in November 1924 it conspicuously came out with a constitutional amendment that the State should never have an Inheritance Tax or income-tax. This State owing to its pleasant climate always beckoned the wealthy to its hospitality and the constitutional enactment added fillip to the move by removing all chances for even the remotest possibility of taxation of the rich. Other States feared that the extra-ordinary temptation offered by Florida might drain them off their millionaires. Another State, this time, Nevada, promptly met the menace by passing a similar legislation in July 1925, and California, ever a rival of Florida as a home for millionaires, could not sleep over the threat. Serious discussions on parallel actions rent the air.

Nothing served the purpose of the advocates of Federal Estate Tax better than such a state of affairs, and the agitation gathered momentum for a thorough survey of the whole position. The administrative defects permeted the State Death Tax system were luridly exposed. The finger of scorn was pointed out towards the bewildering diversity of the existing rates, exemptions and definitions. The exactions of discriminatory practices particularly in the matter of taxing non-resident decedents was thickly underlined. At a meeting of the National Tax Association in September 1924, a resolution was passed that the Association should assemble a

conference of Federal as well State representatives to formulate a scheme for remedying the defects in the death taxation field. The conference in February 1925, attended by delegates from 25 States was addressed by President Coolidge, and it authorised its Chairman, Dr. T. W. Paige, to appoint a committee to report to the next National Conference. The report revealed a fiscal anarchism and dwelt broadly on the perversity of States and their greed for revenue. All sorts of abuses came to light. The greatest of them lay in the practices adopted by the States in taxing intangible property of non-residents. The State of domicile of a decedent always exercised the right to tax the intangibles in his estate. A State might also claim the right to tax the intangibles in the State of a non-resident decedent if these consist of, for example, share of stock of a corporation chartered by it. A State might also claim the right to tax intangibles if these were physically located within its boundaries, for example, in a safe deposit vault or the transfer of intangibles issued by an outside State Corporation and not physically situated within its boundaries if the Corporation had property within the State. In short, different States levied the tax on different bases, each selecting the individual basis which suited its requirements and many States levied it on a multiplicity of grounds.

The Committee found ample evidence of the misuse of death taxes by the States. Yet as Mr. Mellon, the Secretary of Treasury, said in his evidence before the Ways and Means Committee of the House of Representatives, the field of death taxation was considered to be strictly belonging to the states "by tradition, legal theory and revenue necessity." * The Committee was also inclined to the view that a compromise lay in allowing the Centre to continue to levy a death tax but that 80 per cent. of the proceeds should be handed over to the States.

* Hearings, Revenue Revision, 1927-28. P. 13, U.S. 69th and 70th Congress, House of Representatives, Committee on Ways and Means.

In the United States death taxes are also levied by the Federal Government and we have already seen how the Centre had utilized this source of revenue as an emergency measure. The Federal Estate Tax of 1916 which later became a permanently dependable addition to the revenue system of the United States was at first levied under severe fiscal pressure during the World War I. The tax was purposely laid upon the transfer of property rather than upon property from the decedent to others in order to avoid legal challenge or nullification as a direct tax." This tax exempted any estate whose net value was $50,000, and the rate schedule rose upto 10%. "The guiding principles behind the Federal Estate Tax were productivity of revenue in the face of a fiscal emergency, ease and simplicity of collection, and placement of a preparedness tax burden on the wealthy rather than the poor. From the standpoint of the heir against that of the community, an inheritance tax on, and graded to, the shares of the individual beneficiary was preferable to the estate duty, but the difficulties of administration and loss in revenue entailed, impelled the Congress at that time to choose the latter. The burden of the tax was not appositioned among the various beneficiaries according to their respective shares, but fell solely upon the residuary legatees, often the decedent's wife or family, unless the will directed otherwise." *

Within two years, the rates were increased to reach the maximum of 25% on estates whose value was over $10,000,000. This shot up to 40% in 1924. Two years later, the maximum rate was brought down to 20% and the exemption limit was increased from $50,000 to $1,00,000. By 1926, everything was in an utter confusion in regard to the State death taxes as a result of the keen competition that prevailed in the matter of rates, exemptions, etc. Several States did not even impose the inheritance tax, as they feared that the richer classes would desert. The result was that the Central Government was

* Ratner; American Taxation, p. 357

compelled to grant to the States an increased rate of credit, which came to the maximum of 80%. Such a high percentage also gave place to opposition of the attitude of those States which did not levy the inheritance taxes and it was widely contended that this would give a handle to the States to abolish inheritance taxation in toto. In 1926, therefore, though the tax was left untouched, an additional tax, without the previous 80% credit, was superimposed. At last, in 1944, the rates came to be ranged between 3 to 77 per cent., the maximum falling upon the estates being over $10,000,000.

(*d*) Australia

Death duties in Australian States have been reckoned as one of the most important revenue-yielding items. They led the other countries in the adoption of progressive rates which were quite rapid, particularly in the case of the estate taxes. As early as 1866, Queensland had a stamp duty on wills and letters of administration in respect of the Queensland estate of the deceased persons which had to be paid on the personal estate that came into the hands of the executor or the administrator. The act of 1870 which, for the first time, adopted the true estate duty in Victoria provided for an estate duty ranging from 1% on £1,000 to 5% on the value of the estate of £20,000. In 1886, Queensland adopted a progressive estate duty with rates rising from 2 to 5%, while the estate that passed into the hands of the widow and descendants with blood relationship was liable to taxation at half the rates. There were minor amendments in 1889 and 1890 when the graduation was so adjusted as to provide for 39 brackets instead of 9, the general rate of increase remaining the same. It was in 1892 that a more complex classification was called for by which the rates for the surviving spouse in the direct line—from 1% at £1,000 to 5% where the estate was worth above £200,000—were fixed by the size of the estate. Irrespective of the amount of property passed to collateral relations, double the rates had to be

paid, and strangers who inherited property paid quadruple the rates.

South Australia levied her first tax in 1876 which resembled closely the contemporary English statutes with a 1% probate duty on wills and a duty of 1½% in cases of intestacy. Over and above this, a tax on the shares of the decedents graduated on the lines of the English tax, that is according to the relationship of the inheritor to the deceased, was also levied. Within less than a decade it shot up to the heights of a very progressive inheritance tax, the surviving spouses and lineal descendants paying from 1½% on amounts between £500 and £7,000 to 10% on amounts over £200,000, the maximum rate being 10% in respect of legacies or successions of £20,000.

In New Zealand, death duties were first imposed in 1881 at a very progressive rate rising from 2% on the first £1,000 to 10% on the excess over £50,000. In 1885, the progression became steeper, though spouses were exempted and strangers without any blood relationship paid, a higher percentage than the basic rate. In 1909, estate as well as inheritance legislation was enacted, the rates in both the cases being as progressive as before. The estate duty progressed from 1% to 15% while the succession duty followed four-class relationship discrimination according to consanguinity, and one-step progression.

Remarkable changes overtook the Australian States with the impact of the World War. The estate and succession duties in New Zealand have undergone a vital change. The rate of estate duty which started at 1% on the first £1,000 of an estate over a £1,000 exemption went up to 20% on an estate of over £100,000. The succession duty maintained progression on the basis of the size of the estate rather than on the individual's share of the inherited property. The maximum that the strangers and the relatives beyond the fourth-degree had to pay was fixed at 20%, when the value of the estate exceeded

£20,000. Thus, by 1904 almost all the States provided for the taxation of estates and successions, and also of gifts 'in contemplation of death.'

In Australia, the Commonwealth Estate Duty that was imposed in 1914 was based on the lines of the British Estate Duty in so far as the tax was imposed upon the aggregate net value of the estate, real or personal. The Estate Duty Act of 1914 and the Estate Duty Assessment Act, 1914-28, levied a duty on the estates of deceased persons, the net value of which exceeded £1,000. The rate of tax where the value of the estate for duty need not exceed £2,000 was 1%. Where the value of an estate for duty exceeded £2,000, the rate was increased by one-fifth of £1 for each £1,000 or part thereof, in excess of £2,000 to a maximum of 15% on estates over £71,000. Where the estate passed to a widow, children or grand children, the duty was payable at two-thirds of the ordinary rate.

By the Estate Duty Assessment Act, 1940, the Estate Duty Act, 1914-28, was amended to allow the following statutory exemptions:—

a. Where the whole of the estate passes to the widow, children or grand children of the deceased, the sum of £2,000, decreasing by £1 for every £10 by which the value exceeds £2,000 upto £10,000, and thereafter decreasing by one pound for every two pounds by which the value exceeds £10,000;

b. Where no part of the estate passes to the widow, children or grand children, the sum of £1,000 decreasing by one pound for every ten pounds by which the value exceeds one thousand pounds, and thereafter decreasing by one pound for every eight pounds by which the value exceeds £6,000; and

c. Where part only of the estate passes to the widow, children or grand children, the statutory exemption has to be calculated proportionately under (a) and (b).

Under the Estate Duty Act, 1940, the following new rates were imposed:—

£1 to £10,000		3%
£10,0001 to £20,000		3 to 6%
£20,001 to £100,000		6 to 18%
£100,001 to £500,000		18 to 20%
Over£500,000		20%

By the Estate Duty Act of 1941, these rates were later amended as follows:

£1 to £10,000		3%
£10,001 to £20,000		3 to 6%
£20,001 to £120,000		6 to 26%
£120, 001, to £500,000		26 to 27.9%
Over £500,000		27.9%

Under the Estate Assessment Duty Act, 1914-40, provision was made for the exemption of the estates of members of the forces who died on active service or within one year after its termination from injuries received or diseases contracted on actual service, provided the value of the estate did not exceed £5,000. In June 1942, an amendment provided for an exemption of £5,000 in respect of the estates of those members of the forces who died during the War of within three years of its termination, the exemption being restricted to estates passing to widows, children, grand children, parents, brothers, sisters, nephews or nieces of the deceased.

(*e*) Canada

In self-governing Dominions like Canada, the Statute Book bears death duties or inheritance taxes. According to Section 92 (2) of the British North America Act, 1867, the succession dutics were collected only by the provinces in Canada. The tax was imposed by Ontario, Quebec, Nova Scotia, and New Brunswick in 1892, and was later introduced by other provinces as well, slowly and gradually. It was to support the charitable institutions within its jurisdiction that the Ontario Act was first passed. According to it heirs in the direct line were exempted

when the value of the estate was less than $100,000 when it was between $100,000 and $200,000 the rate was 2½% which increased to 5% when it was over $200,000. It was not long when an innovation was introduced in the scheme of 1892. In 1905, an additional duty of 1% was added to tax paid under the estate duty when the share of the estate inherited was between $100,000 and $200,000 increasing to 3% when the share exceeded to $80,000. Ontario utilised the proceeds from this source at first for specific purposes, as in the case of charities, but now it has been provided that the proceeds be diverted to the general fund.

Soon after the Ontario Act was passed, Quebec followed suit, though it provided for five grades of relationship with varying rates. Later, it provided for six-degree relationship discrimination allowing the progressive rates to rise slowly.

The Act of Nova Scotia was almost the same as that of the Ontario, except that the exempted amounts were lower.

In New Brunswick, the rates varied from 2.75% to 25% according to the amount of the whole estate, the amount of individual share and the relationship with the decedents.

In 1914 most significant changes have been witnessed in the field of Canadian Inheritance Tax. Ontario amended her statute with the result that the rates rose slightly in 1915, and exemption was given to direct heirs and soldiers on active service. By the end of the War, rates of the shares of the estate inherited by distant relatives and strangers in blood mounted up. The rate of taxes on the estate, the value of which was about $500,000 stood at 15% and where it was about $22,000 20%.

Quebec, Nova Scotia and New Brunswick increased their rates of inheritance taxes in 1916, 1917 and 1915 respectively. Several minor alterations were also carried out. It is difficult to follow the legislation of all the states from year to year.

The succession duty that was imposed by the Dominion Government of Canada affords an interesting study. It was first imposed by the Dominion Government under the Succession Duty Act, Cap. 14, Statutes of 1940-41, second session, assented to on June 14, applicable to estates of decedents dying on or after that date.* This in its turn was amended by Cap. 25, Statutes of 1942, the amendments being made retroactive in effect to the date of the original legislation. Later, some more minor amendments were made by Cap. 37, Statutes of 1944-45 effective from date of assent (15 August 1944.) This field of taxation had been previously under the control of the provinces and not under the Dominion, though it cannot be said that either of them had exclusive right or monopoly to it. The Finance Minister was of the opinion that "the compelling need for revenue which induces us to enter this new field arises from the war, but I would not suggest that this new Dominion tax is a temporary war-time tax only."

This tax applies to all property of persons domiciled in Canada at the time of death, excepting real estate outside the Dominion of Canada, and upon the succession of all property situated within the frontiers of Canada in cases where the deceased died domiciled outside Canada. The Act expressly mentions that the property owned at the time of death and also certain other property passing at the time of death, transferred by the deceased in contemplation of death, or transferred by gift by the deceased within three years of death etc., shall be included in the evaluation of the estate. The same Act provides also for two forms of duty, viz. initial duty and the additional-duty; the former is determined by the 'aggregate net value' of the estate, while the latter is determined separately for each legacy or bequest which depends upon the relationship of the beneficiary to the deceased and upon the net value of the property, so that the tax assumes the shape of a succession duty. The initial rate depending on the

* cf. Reference Book for Dominion Provincial Conference on Re-construction, "Succession Duties."

aggregate net value began at one half of one per cent. on estates in excess of $25,000 and increased by totality until the maximum rate of 10% was reached on estates exceeding $5,000,000 in aggregate net value.

The Royal Commission appointed in November 1944, to investigate and report "upon the taxes imposed under laws in force in Canada, on income and successions or inheritances arising upon the death of a person owning a substantial proportion of the shares of a private corporation, or a closely held corporation, which had accumulated an earned surplus, and to consider whether under any circumstances there should be an abatement of the tax liability and, if so, under what circumstances and to what extent there should be such abatement." On 29th March 1945, the following recommendations were issued by the Commission:—

1) That the companies to which these recommendations apply be those which, in general, are within the definition of a private company as provided in the Dominion Companies Act;

2) That capitalization or distribution of surpluses earned prior to the end of the 1939 fiscal year be permitted on payment of a special tax by the company, which will approximate the tax that would have been paid by the shareholders had the surplus been distributed year by year;

3) That to accomplish this objective, a graduated rate of taxes be applied to the amount of distribution or capitalization made or accruing to each shareholder—the minimum rate being 15% on amounts up to $25,000 and the maximum being 33% on amounts in excess of $400,000 to any one shareholder;

4) That permission to capitalize or distribute such surpluses be available for a period of two

years from a date that the plan is made law;

5) That the refundable portion of Excess Profits Tax be made available to apply in part payment of the special tax; and

6) That on the reorganization of a private company which involves a change in beneficial ownership or on the winding up or discontinuing of business of any such company, the undistributed income which is deemed to be the payment of a dividend under the present law, be reduced by an amount equal to 20% of the income after tax earned in 1942 and subsequent taxation years.

All the changes in succession duties in the various provinces had been designed to increase their yield and to define more clearly properties subject to taxes.

In Quebec, the current Legislation under Cap. 80 according to the revised statute of 1944 fixed the rate of duty on the net value of the estate, the relationship of the deceased to the beneficiary and the amount passing to each individual beneficiary—the beneficiaries being divided into three classes. In Ontario, the current legislation is Cap. 1., statute of 1939 as amended, the rates of duty depending upon the same principles as in the Quebec Act.

The revenue from succession duties in all provinces showed a remarkable increase in 1921 as compared with that of 1913, and a further rise was seen in 1939. Although the changes in the rate structure and other factors had made the death duties highly productive, the increase suit, on the whole, was not proportionately as great as the general increase in the provincial total tax revenues. But death taxes did contribute a much higher proportion of total provincial revenue in Quebec and Ontario than in other provinces, the percentages for 1939 being—21 in

Quebec and 13 in Ontario—while in Manitoba it was only 5.3%.*

(*f*) U. S. S. R.

Prior to 1649, the inheritance of landed property was liable to taxation in Russia by a duty of 1½ copecs per 'tchetvert' on property. † This underwent several changes in the 17th and 18th centuries, the two most important of them being the exemption of heirs in the direct line (1775) and its abolition (1801). Seven years later a 6% collateral tax was levied and was later extended to inheritances between spouses. Despite several attempts at developing the inheritance tax to fall on movable and immovable properties and to include collateral discrimination on a four-class basis, the move was bitterly resented by the nobility. The proposal was once again revived with rates from 1½% on heirs in the direct line and 8% on heirs beyond the fourth degree of collateral relationship. ‡ Exemption was made for peasants in respect of the transfer of landed property, agricultural buildings and implements. Till 1905 no important change was introduced in the rates. The previous rates were however increased by 1½ times owing to the outbreak of the Russo-Japanese War. It later provided for the escheat of a decedent's property, providing for a moderate allowance for survivors to the estate.

The former inheritance tax is now replaced by a special levy, varying in accordance with the value of the property inherited. The duty imposed amounts to 20% on property from 300 to 1,000 roubles in value and 10% on all property exceeding 10,000 roubles in value.

Even in a country like *the U.S.S.R.*, where private property does not exist except in the narrow, sense, the inheritance taxes though playing a less important role continue to exist.

* Reference Book for Dominion Provincial Conference on Reconstruction, Succession Duties.

† Garvlli, L'Impostea Successoria, page 145.

‡ Shultz, The Taxation of Inheritance.

(g) France

In France, the transfer of immovable property on on the death of its owner was subject, according to an Act passed in 1703, to a moderate transfer tax which exempted any transfereance of property to direct heirs. A revision of the system of taxation as a whole brought in several changes. The Registry Act of December 1790 introduced provisions that the direct line could be taxed ¼% on the inheritance of movables and immovables, while the surviving spouse paid 1%. While those persons with blood relationship paid 2% on movables, decedent collaterals and strangers paid 3% and 4% respectively.

There was a great discussion when 'Code Napolean' had come to be drawn up. The matter was referred to the 'voix de la nature,' and no changes could be brought about. The Act of 1816, put more weight on succession than on transfer. This was followed by another Act of 1832, which made this collateral classification with rates on movables from ¼% in the direct line to 6% on strangers, and from 1 to 9% on immovables.* The distinction was long kept up and it was only after a period of 18 years that it was discarded. A progressive rate was introduced in 1884 which rose to 50% in cases of inheritances above 5,000,000 francs. Not all the protestations of the conservatives could be of any avail when a progressive inheritance tax was voted for by the Chamber of Deputies in 1895. But the Act was not finalised until 1901; its salient features were:

1) The rates were progressive by bracket;
2) The tax applied now to the net instead of the gross estate;
3) In the case of life estates and remaining interests, the tax was apportioned with a crude approximation of the life tenants' expectation of life; and
4) Provisions to strengthen administrative procedure

* **Shultz:** The Taxation of Inheritance, p. 28.

and to check fraud and evasion were incorporated.*

Once the Act was passed, the socialist bloc in the Chamber of Deputies grew more insistent in its demands that any increase in the military expenditure had to fall on the taxes on inherited property, with the result that the Minister of Finance could propose a general increase of rates in 1905 above 10,000 francs, but discrimination amongst the different classes of inheritors was not observed till 1910. In 1914, efforts were made to pilot a special Estate Duty Bill. Several amendments were proposed to increase the revenue by instituting an estate duty, but no change could be effected in the existing inheritance tax rates until a finance bill was passed in December, 1917. This Act had three important features—

1) A sharply progressive succession duty with deductions and exemptions allowed to heirs with large families;
2) A special estate duty which was progressive and graduated according to the number of children of the decedent; and
3) A gift tax with a complicated graduation.

More and more pressure was being exerted on revenue for military purposes, and the socialist influence which was so vigorous, could at last bring about a sharp increase in the rates of both the inheritance tax and the special estate duty in 1921. No other important change was later effected, except in the matter of increasing rates according to the revenue needs of the day.

(h) Italy

Under the Napoleanic occupation, the French Enregisterment Tax was imposed in Italian States. This was extended after 1815 in several States, but the complexity in the matter of rates and exemptions called for systematization of the various inheritance taxes. It was in 1862 that a Tax Law closely resembling the contemporary

* See a detailed survey of the Act of Emily Georges Nicolan, p. 48.

French Law was adopted. In 1889, the first proposal was made to fix the rates on collateral inheritances which increased from 5% to those under 25,000 l. to 20% when the aggregate value was about 100,000 l. The Tax Law of 1902 had some progressive features, but the rates remained upchanged till 1914 when Minister Giolitti proposed an estate duty that rose from 1% on estates of 10,000 l. to 6% on those estates of above 10,000. l.

Irrespective of the fact that inheritance tax has been utilized as a resourceful fiscal instrument, the Italian States continued to depend on indirect taxes than on the direct. Because of the socialist influence, the rates of the inheritance tax were, by a Royal decree (November 1919) increased so that the direct heirs paid 12% on 20,000,000 l. brothers and sisters 26% and strangers 50%. Soon after the Nitti Bill again increased the rates of the inheritance tax. Several proposals for a strict application of this tax as a socialist measure were in the air, and the State had been given power to confiscate any excess of of the maximum of 100,000 l. The celebrated Italian economist Rigno after considerable thought to the proposals, came to the conclusion that a part of the estate which was received by way of bequest or gift should be confiscated by the State. He also proposed that every State should be divided into two categories, one to consist of value equal to the amount the decedent had inherited or received as a gift during life time, and the second of the amount which the decedent had saved by the sweat of his brows. With the coup d'etat the whole structure of Italian taxation underwent radical revision. Family members including uncles and nephews were exempted from the tax and a single progressive rate, ranging between 12% on the first 10,000 l. and 50% on the excess of 10,000,000 l., was maintained for those decedents without any successors with blood relationship. Shultz in his "Taxation of Inheritance,' says that "this extreme reform with the great loss of revenue involved, has been defended by Fascisti on three grounds:

1) It strengthened the institution of the family, which is the foundation of national unity;
2) Evasion by estates consisting largely of intangibles had thrown the burden of the tax under the previous Act on landed property, so that the reform would work greater justice between social classes; and
3) Since the movable wealth of Italy was concentrated in the northern provinces, the reform would assure greater justice between geographical divisions."

(i) GERMANY

Inheritance Taxes in one form or another were levied in some of the German States during the 17th and 18th centuries, the most important States being Hamburg, Bremen and Leubec. The Hamburg Inheritance Tax was first levied in 1628 at a flat rate of 5% on all successors who passed beyond the third degree of relationship. By 1830, the tax was extended to those with blood relationship of the decedent with a rate of $2\frac{1}{2}\%$. In Bremen it was not until 1807 that a true inheritance tax was instituted. Those of the direct line of descendants were exempted from the tax and one step of collateral discrimination was adopted soon after by taxing brothers, sisters, nephews and nieces. Leubec introduced her inheritance tax in 1820. Within two and a half decades, the tax structure had four separate tax rates for all the grades of colleteral relationship.

In Germany, there were two schools of thought: the one receiving its inspiration from Ricardo and the English school and emphasizing the danger of the destruction of capital but mildly approving the tax as long as its rates were low; and the other defending the inheritance tax as in element of the Stat's rights to be considered an heir of every decedent.* In 1842, this idea of the inheritance rights of States was developed by Paul Achatius Pfizer, who did not favour unearned succes-

* Shultz, The Taxation Inheritance, p. 53.

sions of wealth which he suggested should accrue to the State. The rates of inheritance taxes from year to year seemed progressive but it was not till the Hamburg Law of 1903 was passed that a real progressive inheritance tax was levied. No important change took place in the administration of the inheritance tax at all till 1919 when the Government was, under financial exigencies, compelled to resort to a heavy tax programme. The Act of 1919 contained some provisions by which the previous wealth of the heir was taken into account in the determination of the rate. But this was found to be of no avail, as evasion became quite rampant. The real foundation of the 1919 Inheritance Tax in Germany was not that of their estate duty but one of individual legacies and successions. The limit of exemption was put at 5,000 m. to all persons in the direct line of descendants. To those who had been bearing blood relationship, the exemption was put at 500 m., but the full rates embodied in 1919 Inheritance Tax did not apply till 1935.

SUMMARY

Death Duties are one of the earliest recorded taxes, which originated in Egypt seven centuries before the Christian Era, and have gradually become a regular fiscal instrument in almost all the countries except however in India. In the U.K., the estate as well as the succession duties are leveied by the central government. In the United States, death duties are imposed both by the Federal and the State authorities. In Australia, these taxes are levied by the Federal Government and also by each State. In general, Australian legislation imposes those that are of the type of estate duties rather than that of the succession duties. In Canada, inheritance taxes form part of the provincial field, despite the fact that the Royal Commission on Dominion—Provincial Relations desired that it should be solely a federal item. The history of probate duties in India, and death duties in U.K., U.S.A., Australia, and Canada, U.S.S.R., France, Italy and Germany has been dealt with in detail in this chapter.

CHAPTER 4

Theory of Death Duties

1. Classification of Death Duties, 2. Characteristics of Estate Duty and Inheritance Tax, 3. Justification of Death Duties, 4. Theories Against Death Duties, 5. Summary.

> *Death duties are.....''a source of revenue which should be considerably developed. Inherited wealth is wholly unearned and, in excess of a moderate amount, it encourages idleness and thriftness in its recipients. It is, therefore, a peculiarly approporiate object of, taxation''.*
>
> Dalton in his evidence before the Colwyn Committee

1. *Classification of Death Duties*: Death duties are levied on the occasion of transfer of property of the deceased at the time of his death, and can be classified into three categories:

(1) Estate Duty

(2) Legacy Duty

(3) Succession Duty.

Estate Duty is payable on the entire estate left by the decedent at the time of his death, before distribution, irrespective of the share which the inheritors obtain. Legacy Duty is imposed on the actual benefit accruing to the legatee wherein the rates are determined solely by the relationship of the beneficiary with the deceased. Succession duties are "charged not upon the whole corpus of an estate but upon the interest which a person derives from property left to or devolving on him upon death." Levies are not made on the corpus of the estate but upon the interest which the legatee or the successor thus derives from property devolving on him at the occasion of death. Legacy duty is only payable on personal property under wills or intestacy, while succession duty is payable on gratuitous acquisition on death. But the main death duty levied is the Estate Duty chargeable on the whole

estate left by the deceased while the Legacy and Succession duties leviable on property inherited by the successors is a minor one. The broad classification of death duties, however, consists of firstly, estate duty and, secondly, inheritance tax, the former being levied on the total estate left by the decedent and the latter being imposed upon the individual share of the inheritance after distribution among the several beneficiaries. In addition, an inheritance tax based on the inheritance according to the wealth the inheritor possesses at the time of the death of the decedent, can be visualized.

2. *Characteristics of Estate Duty and Inheritance Tax*: We have seen in the first chapter important characteristics prerequisite for any sound and well-designed tax system. We shall follow the same criteria in the matter of the two components of Death duties, and see how far they are satisfied by them.

(i) *Tax Adequacy*:—Death Duties are very productive, and have been contributing their utmost in the fiscal armoury of several countries. The minority note to the Clowyn Committee Report embodies the view that "death duties are a most valuable source of revenue of which by no means adequate use has already been made." But taken individually, from the point of view of tax adequacy or productivity, it has been the experience of all the leading countries of the world that the estate duty is a better revenue-producer than the inheritance tax. Estate duty falls upon the total property of the decedent, while the inheritance tax is levied upon the share of property ing uniformity in the matter of exemption, although it may differ according to the number of dependents and their relationship to the deceased. Steep progression in rates can also be followed in the case of an estate duty than in inheritance tax, for in the latter, there will have to be an elaborate classification of heirs and graduation is more complicated than in the former. H. M. Groves writes: "The estate tax is simpler and more productive than the inheritance tax. It avoids entirely the exceedingly complicated task of determining the value of shares

where the transfer involves life estates, contingencies, and remainders. The inheritance tax, on the other hand, gives special weight to the ability to pay of the heir, although if his circumstances apart from the inheritance are not taken into account, the measure of his ability to pay is incomplete. Inheritance tax rates are often deceptive; they may appear very high in the top brackets, yet the average effective rate of the tax on all transfers may be very low." * Moreover, "there is no splitting up of the estate and a consequent reduction in the brackets taking the higher rates; and there is only one tax to compute, which may be paid out of the estate in its entirety, letting the incidence upon the various beneficiaries be what it may. The inheritance tax, on the other hand, is more readily capable, by means of exemptions and adjustments in the rate structures on the different classes of beneficiaries, of conformity to abstract justice, and of effecting social consequences that may be desired."† Estate duty is more productive than inheritance tax; and there is less possibility for evasion in the former than in the latter. Findlay Shirras, says : " evasion is less easy under an estate tax than under a succession or inheritance tax, where collusion may take place on the part of the executors of the beneficiaries regarding the relationship of the decedents and the beneficiaries in order that a lower tax rate may be levied. An estate duty, however, may also provide for discrimination in regard to relationship, and if this were so, would be subject in this respect to some degree of evasion. The mere fact that the higher the value of the estate the higher the rate of duty leads to much higher returns of duty in the upper reaches of estate valuations than would be possible under the inheritance taxes where the estate is broken up before reaching the beneficiary." †† Thus it should be maintained, beyond doubt, that estate duty is simpler and conforms to the sovereign characteristic of tax-adequacy better than the

* H. M. Groves; Financing Government, p. 221.

† Jensen: Government Finance, p. 405.

†† Findlay Shirras: Science of Public Finance, p. 524.

inheritance tax, as the taxing authority can estimate the revenue-yielding capacity of the estate duty, as vagaries in individual will-making are not involved, and moreover, the duty conforms to the fiscal justice in the case of collateral graduation and progressive rates on the individual beneficiaries, unlike the inheritance tax, which cannot prescribe highly progressive rate schedules on the upper brackets. Same is the experience of countries like France, Germany, and U.K.

(ii) *Equity in burdens* : That the tax system should be equitable and fair has been recognised all the world over. Equity in burdens can be tested with the touchstone of ability. The inheritance tax falls upon those who receive property as a windfall. It also falls on the property which can be often characterized as "unexpected" and "undeserved," and it indissolubly bears discrimination among the heirs of the deceased on the basis of their relationship. It would bear levels of exemptions discriminating between the direct and indirect heirs. All the heirs of the decedent, irrespective of their relationship cannot justiciably be made to pay the same rate of progression of the tax. Those who inherit property from the deceased and who do not bear blood relationship with the decedent have more ability to pay inheritance tax than the heirs who are direct descendants.

On the other hand, estate duty cannot comply with the canon of equity, as "the graduation of the estate duty is only accidentally and uncertainly related to the ability to pay of the successor. The beneficiaries may be rich or poor; there may be one, there may be several. Such considerations do not affect the duty; an estate divided among several children pays no less heavily than an estate of the same size passing to one; a poor beneficiary suffers as heavily as a millionaire on a benefit of the same amount." * To that extent, the estate duty is unequal than the inheritance tax. Both Schuster and Cannan, therefore, favoured the taxation of the inherited

* National Debt & Taxation Committee Report, 1924-27, Para 490.

share rather than the entire estate. Moreover, "the estate duty or tax is inequitable as between comparable estates when deaths occur more frequently in one than in another." † This argument has been originally advanced by Adam Smith, in his *Wealth of Nations* : "Such taxes, even when they are proportioned to the value of the property transferred, are still unequal; the frequency of transference not being always equal in property of equal value." †† Even supposing that there would not be much differentiation in the rates, it is most likely that the value of the property of some persons might appreciate while that of the others might remain stable or even fall. Estate duty cannot therefore be blamed, for it is the same case in all forms of taxation and it is not peculiar to estate duty only.

From equity in burden, there is a good defence for estate duty, though several writers have criticised the inability of the duty to distinguish between wealth inherited by the decedent and wealth accumulated by him as a result of his own exertions. It might be said that even the income tax suffers from the same serious defect, but the seriousness in the case of estate duty is less. The discrimination between the property saved by the deceased and that inherited by him, or bequeathed to him by way of gifts, can however be maintained by the rate of progression of the estate duty.

(iii) *Simplicity, Certainty and Economy in Administration and Compliance* :

Taxation should be sufficiently simple so as to obtain the willing co-operation of the tax-payers. Confusion should be avoided as far as possible, particularly in the selection of the tax bases. In the case of death duties the rates are often based on the nationality or the citizenship of the decedent or the beneficiary, the situs of the property inherited, the degree of relationship, etc. The

† Findlay Shirras: Science of Public Finance, Vol. II p. 533.

†† Adam Smith: Wealth of Nations, Book V. ch. ii, Appendix (Canada Edition, Vol. ii. p. 37).

multiple bases for the death duties introduce much complexity and cause confusion. In the case of estate duty, it is simpler than the inheritance tax, as the latter falls upon the inheritors and depends upon the share of each successor, either in conjunction with his relationship to the decedent or independently.

Closely related to this is the canon of certainty. Simplicity and certainty go hand in hand. When the time of payment of any tax and the amount to be paid are fixed the tax possesses the characteristic of certainty. As the tax falls directly or indirectly on the beneficiary or the inheritor, its payment is quite certain. The successor knows that the tax has to be paid at the death of decedent and the transfer of the property. It is also convenient for the beneficiary to pay the tax, at the transmission of property.

Economy in the matter of administration and compliance is a very desirable characteristic of a well-designed tax system. The administrative cost of the taxing authority should be as low as possible, and the government should obtain the maximum of revenue from the tax with a minimum of cost. Evasion and avoidance should also be prevented. The estate duty satisfies eminently the canon of economy, and it is simpler and more productive than the inheritance tax. According to Adam Smith, estate duty is "perfectly clear and certain" and the time of payment "sufficiently convenient." It is easier, simpler, more certain and economical to collect estate duty rather than the inheritance tax.

(iv) *Economic Soundness* : That the tax system should be devised so as to minimise the obstacles in the way of economic progress and to maximise economic stability is quite apparent. This principle is satisfied by both the forms of death duties and, more so, by estate duties. The estate duty will not have any serious repercussions affecting the economic development of the country, and its effects in so far as they result from the estate taxation will be socially beneficial as it attempts at equalization of wealth. There cannot be any doubt

that the inheritance tax is economically sound especially when the ability of the inheritors to pay is great. Consequently, the tax can be paid without any burden. But looked at from a broader angle, it will be clear that the economic soundness of the estate duty, which is more productive and which has often one exemption, satisfies this canon better than the other.

Admittedly the estate duty is more productive, the inheritance tax is more just, as it satisfies the principle of taxation according to the abilities of the tax-payers. "Where the governmental agency, be it state or federal, looks upon the tax on inherited wealth as an incidental source or income which is to be diverted into some special fund, or where such governmental agency feels that in view of the rest of its tax system it is not forced to abstract every cent possible from the tax on inherited wealth, then the inheritance tax on the shares of the individual beneficiaries is certainly advisable; in so far as abstract justice is desireable or attainable in taxation, it is more fully embodied in the inheritance tax than in the estate duty. Where, however, a certain and large revenue is the primary element, the estate duty may be preferable; an estate duty can always be made to produce more than an inheritance tax unless the latter's rates are made relatively much severer. The injustice involved may be offset by the possibility that the additional revenue would otherwise have to be raised from other sources that are from a social point of view less desirous and more inequitable."

Justification of Death Duties:

Several arguments have been adumbrated in justification of Death Duties. We attempt below a study of them:

Ability to pay theory: Death Duties conform to the principle of ability to pay. It is a sovereign canon and guides the taxing authority in all its deliberations. The ability of a person to bear the brunt of the tax depends upon the size of the income, and the taxable capacity of

* Shultz: the Taxation of Inheritance, p. 220.

the individual increases more than proportionately with rapid expansion in his income. But in the case of Death Duties two arguments can be adduced. On the one hand, we find a person has, by the sweat of his brow, accumulated property and on death he ceases to have any more earthly rights on the same. On the other hand, there is the beneficiary or the inheritor or the successor of the decedent's property. Either because of the latter's blood-relationship, near or distant, or on the strength of the will of the deceased, the beneficiary could claim the property as his own.

Death duties are payable only after the death of the decedent. Only in cases of bequests or gifts "in anticipation of death" will the tax load fall on him. To that extent then, there is some justification of the ability of that person in paying the tax on bequests or gifts. Although the tax is borne by the deceased, it is clear that it is collected at the most supreme time of tax-paying ability—that is, on the occasion of his total disappearance from the physical world. As his interests cease wholly in the property acquired before his death, there is substantial justification in the ability theory. Once a person dies, he does not have to bear the tax-load. Thus incidence of the duty can hardly reach the decedent. Objection might be raised to the effect that the decedent prior to his death might have made certain arrangements for the payment of the tax. He might have been imbued with the idea that such a provision would stand by his heirs. That is, he might have insured his life in the hope that the insurance company would foot the death duty bill and thereby leave his heirs free from all botheration. This is not a sound argument. A person might insure his life for several reasons, chief of them being that the heirs would not have any difficulty to get going their routine without any financial exigencies with the death of the head of the family, but the insurance method is never used to cover payment of the death duty. Moreover, a percentage of the decedent's property can, without any hesitation be paid by the beneficiary, and the deceased need not be worried on that account. Taking

the insurance method for what it is worth, we find that these death duties assume the form of an annual property or income tax with deferred collection.* The assumption that the decedent would, with the aid of the insurance try to stint and save to the fullest extent necessary for the payment of death duties does not hold in the cases of small as well as big investment incomes alike. As will be evident later in "Incidence of Death Duties", the insurance method is possible in the case of small investment incomes, but even then, the supposition that the property-owners save only so much to meet the death duties does not correspond with the existing facts. At a later stage, it will be quite apparent that even where the possibility exists as in the case of the small investment incomes, it is not the usual practice.

There is the other aspect of the ability theory, which regards the death duty as a direct tax on the beneficiary. If the tax is not borne by the deceased, as it is not the case, the recipient of the inheritance has naturally to pay the duty, and when it is considered to be falling upon the beneficiary, it devolves upon the property or the estate that has been inherited by him. "Inherited wealth is in the nature of a windfall. Beneficiaries and heirs have not earned it and have no right to it other than that created by state statutes of descent and bequest. Furthermore, until they receive their shares from the executor or administrator of the estate, the taxed property does not belong to them and they cannot be considered as burdened by any taxes upon it." † It cannot be disputed that the addition to the wealth of the beneficiary or the inheritor by the amount of inheritance earmarks the ability of the tax-payer. The inherited portion of the property is a form of income, though not a regular periodic return, but "it is an irregular, a spasmodic, a chance return." †† There cannot be any favourable comparison between a death duty and income-tax. While the former is irregular because of the uncertainty of the time of death, the latter is

* Harold M. Groves: Financing Government, p. 228.
† Shultz: American Public Finance, p. 489.
†† Shultz: The Taxation of Inheritance, p. 189.

a regular annual tax; while the former falls upon transfers of property at death, the latter is imposed upon the regular incomes of an individual.

The accidental income principle, according to Seligman, regards the inheritance tax as a personal tax, payable by the person who happens to be the recipient of the property. The unexpected character of the accretion to property lends colour to the ability theory, and the taxpaying ability of the heirs varies so much, as it depends upon the degree of consanguinity of the heir. Direct heirs as well as collateral heirs do not show the same ability to pay the death duty. Those heirs in the direct line cannot be deprived of expectancy of their reasonable claim to the property of the decedent, and particularly in those cases where the survivor happens to be the spouse or children, the ability to pay the tax cannot be so much as in those when the recipient suddenly finds himself to be the owner of property. Thus while inheritance by itself gives some measure of ability to the beneficiaries, on the whole, individual abilities vary. Hence modern inheritance laws embody exemptions in the case of property left to direct heirs, and impose a steeply progressive inheritance tax from the collateral heirs. Thus the principle of differentiation in the taxation of inheritances with exemption, makes it possible for a just distribution of the tax burden on the different heirs. One point need not be overlooked: apart from the inherited property, the survivors' ability should be construed by taking into consideration the wealth they might themselves have accumulated. The tax that has to be imposed upon the recipient who previously possessed much property should be more progressive than in the case where one who has not to his credit sufficient property is taxed. The inheritance and the beneficiary's prior wealth should be the dual factors to guide the public authorities than the size of the share of inheritance alone. In other words relative taxpaying ability of the heirs cannot be determined exclusively by a reference to the shares of the inherited property. As Shultz observes: "the share of an estate received by a beneficiary or an heir rarely constitutes his entire wealth, so that rate of prog-

ression based solely on the size of his share cannot by any theory approximate his taxpaying ability. Surely, a millionaire who receives a one-thousand-dollar bequest has a relatively greater taxpaying ability than a pauper who receives a fifty thousand dollar bequest. Yet under a progressive inheritance tax the latter is taxed more heavily than the former."* As the ability varies, the rate of progression naturally changes, and when the rate of progression is made to conform to ability, death duties are adequately justified. In that case the distribution of the tax burden would be just, and in accordance with the principle of ability to pay. Unless taxes are levied coincident with the inheritances of property occasioned by death, ability to pay the tax escapes the attention of the public authority, and to that extent tax justice as a whole, does not prevail. As the Committee on Postwar Tax Policy in their "Taxation Programme for a Solvent America" observed in 1945, "ability to pay is not a purpose of taxation, but a rule for its distribution." Thus ability affords a meter to measure the validity of an instrument of taxation. With all the limited possibilities for progression, exemption and graduation according to the relationship of the heir, death duties can be more than justified from the point of view of the ability to pay. Sir Stafford Cripps, presenting his Financial and Economic Statement to the House of Commons observed on 6 April, 1948, that "it has long been the practice to tax capital by means of Death Duties, which together with surtax and the high ranges of Income Tax, represent the taxation of wealth following the general principle of fixing taxation in accordance with the ability to pay."

In the case of inheritance taxes, a greater degree of justice is found than in the case of estate duties.

The estate duty does not fully correspond to the ability theory, as it is levied on the aggregate value of the estate, without any regard for the shares of the heirs and their economic status. Thus it is often presumed that the ideal death tax would be of the inheritance type. †

* Shultz: American Public Finance, p. 482.
† Henny C. Simons: Personal Income Tax.

While in the former case, estates of the same value are taxed at rates without any special reference to the number of dependents and their individual economic status, as Buehler says, "the great variations in rates and exemptions in the inheritance taxes imposed by different governments reveal a striking disregard for variations in individual ability and a greater concern for the fiscal needs of governments and what 'the traffic will bear.'" *

Service Theories:

Some *quid pro quo* theories have been advanced to justify death duties. By *quid pro quo* is meant that one thing is paid for another. Whenever a levy is made, it should be able to give some specific service. Thus service theories, which embody the *quid pro quo* principle may be of two kinds: cost of service theory, and value of service theory.

Cost of Service Theory:

Cost of service theory is a very antique form of the *quid pro quo* doctrine and is embodied in Probate Fee Acts of a country. It treats the death duty or, to be more precise, the inheritance tax, as a fee which is paid by those inheritors of property that utilize the services of the probate courts. The probate courts which involve some expenditure to the government levy duties and, only those persons who utilize the service of the government, pay to the extent of the cost of the service. The inheritance tax accordingly should be restricted to a light probate fee and it might not result in a form of tax on transfer of property as such rather than a system of probate fee. The duty levied on probates should not also exceed the cost of service to the government. Cost of service theory cannot be a sovereign determinant of taxation and "the essence of a tax, as distinguished from other charges by government, is the absence of a direct *quid pro quo* between the tax payer and the public authority." † Thus, a tax cannot be imposed with reference to any specific

* Buehler: Public Finance, p. 455.

† F. W. Taussig: Principles of Economics, Vol. II, p. 535, Fourth Edition.

service, and much less in the case of death duties, wherein there is no cost of service involved. The most important objection against this theory is that this charge is very regressive inasmuch as the duty imposed diminishes with the increase in the size of the estate inherited. Naturally, it would mean a denial of tax justice. It cannot also take into consideration the discrimination of relationship that has to be pursued in death duties. The direct heir should not be expected to pay the same rate of progression as the collateral heir. The basic fact, thus remains, that the rates of death duties, either of estate duty or inheritance tax, do not even in the least conform to the cost of service, as it is meaningless to talk about the cost of service involved.

Value of Service Theory:

By value of service is meant the value of the service done by the public authority to individuals. To be more precise, any levy or imposition that takes into consideration the value of service cannot be justifiably and logically taken under the head 'tax'. This principle might stand on a better footing than the cost of service, but an inheritance tax based on this theory would prove to be a very meagre and unjustifiable levy and, neither can progression be followed in the fixation of the rates nor can any appreciable level of exemption be pursued. The tax in consequence would lose its primary characteristic, that is productivity, and once it denies the public authority the revenue it naturally needs, justice in taxation would disappear altogether. Services by the government do not take into consideration the protection that is accorded to the property of the decedent, as Lloyd George made out a case for increased death duties in 1910, as a payment for "the security insured for property by the agency of the state, the guaranteed immunity from the risks and destruction of war insured by our natural advantages and our defensive forces." Though the value of service principle in the case of inheritance tax is appreciable, it provides no basis for the levy of the estate duty. On the

whole, it is a theory which lends a little weight in the levy of tax in general and death duties in particular.

Privilege Theory:

It has been contended by some legalists that no natural right can be established for bequests and inheritances. Transfer of property has been looked at as a privilege accorded by the inheritance laws of the state, and whatever the state grants in the shape of laws, it might deprive the inheritors of the same, by another set of laws. Inheritances and bequests have therefore been looked at from the angle of privileges that the beneficiaries enjoy under a government. The state has every right to demand a duty from the beneficiaries for the privilege accorded to them. As Shultz remarks, "clearly this doctrine allows the widest possible latitude in the levying of inheritance taxes; if the '*quo*' of the state—the privilege to receive or transmit inherited property—is equivalent to the value of the property in question, then the '*quid*' that can be demanded from the heir or deducted from the estate is limited only by the value of that property."* This theory does not provide any basis for death taxation since the privileges attached to bequests or inheritances are afforded by the public authority. But, on the other hand, it is argued that inheritance is a natural right and, as such, cannot be interfered with by any public authority with the effect that taxation cannot be imposed on transfers of property. We have developed this point at a later stage when we argue against the levy of death duties.

Silent Partner Theory.

It has also been said in defence of death duties that the Government is a partner in the accumulation of the property. The estate of the decedent, therefore, has been considered to be a social product. This maintains that an individual can accumulate an estate only by reason of the business milieu afforded by the state. It is, therefore, agreed on all hands that the state is entitled to take a portion of the property even before it is transferred to the

* Shultz; The Taxation of Inheritance, p. 183.

beneficiaries. Gladstone arguing in favour of these duties said: "The carrying of property in perfect security over the great barrier which death places between man and man is perhaps the very highest achievement, the most signal proof of the power of the civilized institutions. . and an instance so capital of the great benefit conferred by law and civil institutions upon mankind, and of the immense enlargement that comes to natural liberty through the medium of the law, that I conceive nothing more rational than that, if taxes are to be raised at all, the state shall be at liberty to step in and take from him who is thenceforward to enjoy the whole in security that portion which may be bona fide necessary for the public purpose."†

The state is, therefore, a silent partner in the accumulation of the fortunes of every individual. "The State . . . is represented as a silent partner in the business of each citizen, without whose aid and protection it may be impossible to transact business or amass wealth; when partnership is dissolved by death, the silent partner is entitled to a share of the capital."* This argument has been the backbone of several economists. According to it, the share of the state in the accumulation of fortunes of the individuals becomes relatively greater in larger fortunes rather than in smaller ones. A death duty is in consequence, considered merely as a state's method of collecting its share in the co-partnership. But taking for granted that a part of the accumulator's wealth is due not only to the efforts of the individual but also the efforts of the silent partner, that is the state, the duty can be viewed as an unearned increment (as in the case of rent of land). It cannot be gainsaid that the state is entitled to any slice or portion of the estate transferred at the death of the decedent.

Back Tax Theory:

Another recent theory in defence of death duties is on the ground that during the life-time of the decedent

† Hansard Vol. C XXXII, 267, 1873.
* West; p. 201.

several taxes imposed on property and income might have been evaded or avoided by him. Taxes might not have reached that particular property and income, which have been accumulated without taxation. It is also argued that a person who accumulates a fortune could be presumed to have avoided some legitimate taxes. Mr. Nichols justified death duties as "the only practicable means of reaching the great mass of personal property consisting of stocks, bonds, notes and other easily concealed objects which readily escape the annual assessment but which must, when the owner dies, pass through the probate court and are then exposed to official examination."* The taxes that have been avoided by the decedent during his lifetime must ultimately be borne by the heir who inherits his property. The ability of the heir is not given due consideration as the tax is imposed without any reference to his ability. It is also difficult to prove the relationship that exists between the beneficiary and the decedent. Any system of progression usually followed in the levy of death duties,—progressive according to the relationship of the inheritor to the testator,—cannot be pursued when the death duties are imposed as the so-called back taxes. According to Seligman, the inheritance tax levied in conformity with this principle would be necessarily confined to personalty, since real property cannot evade its share of taxes so easily. † He points out that where there is a property tax or an income tax, there may be some provision for an inventory of the estate after death with penalties for the evasion of back taxes. That provision is dependent upon inheritance taxes. If death duties are based upon the theory of back taxes, there is little justification in favour of inheritance taxes, while estate duties have more justification. A somewhat broader view is that "The inheritance tax may.....be regarded as in lieu, not of taxes which have been evaded, but of taxes which have not been imposed; that is, as a property tax

* Nichols: Taxation in Massachusettes, p. 523.
† Seligman: Essays on Taxation.

or. . . . a capitalized income-tax, paid once in a generation instead of once a year. It is paid after the death of the tax-payer, and hence at the time most convenient for him; or it may be considered as being paid by the heir in advance." † German economists favour this view, while the English economic experts view estate duty, more or less, as a capitalized income-tax.

Unearned Income Theory:

The amount of property inherited by the beneficiary can be considered as an unearned income. As H. M. Groves said: "He seldom has rendered an equivalent to either society or the decedent which would ethically justify a future claim on his part upon the productivity of society." The unearned income might not be expected and the inheritor would not mind any progressive death duties levied for "hardship depends upon disappointment; disappointment upon expectation; and if the law of succession levies nothing, he will not expect anything." * The differentiation between earned and unearned income is a sound one, and death duties enable a better fulfilment of it. In fact, the concept of death duties as a deferred income-tax on unearned incomes was prevalent in the United Kingdom when it was first imposed. It takes into consideration the ability of the inheritor to pay death duties; and to a great extent, fulfils the function of taxation as a socio-economic measure.

Diffusion of Wealth Theory:

Silverman says that "taxation on property passing at death presents many attractions to the fiscal administrator, for it yields a considerable revenue with comparatively little difficulty and expense. But it appeals also, and with growing force, to those who would use taxation as a means of rectifying our social ills." †† Death duties have thus been favoured as correcting, to some extent, the

† West, p. 205.

* The Works of Jeremy Bentham, Willam Tait, Edinburgh, Vol. II, 1843, p. 589.

†† Silverman: Taxation, its incidence and effects, p. 182.

social inequalities and the transfer of property which largely increases the inequality of incomes, affords an opportune occasion. Death duties are based on the function of the government to utilize its power of taxation as an engine for social reparation in correcting the economic inequalities and in bringing about a more equitable distribution of wealth. Bentham was the originator of this theory of diffusion. The socialists look at this as if it is an agency for introducing state socialism. As J. A. Hobson wrote: "It might be a thoroughly sound policy for the state by taking the taxes in the form of securities, to become part owner and controller of the great business of the country." † But it cannot be dismissed because it is a socialist doctrine. J. S. Mill, accepting Bentham's reasoning as enlarging the boundaries of this theory, wrote: "that no one person should be permitted to acquire by inheritance more than the amount of a moderate independence. In a case of intestacy, the whole property must escheat to the state: which should be bound to make a just and reasonable provision for descendants, that is, such a provision as the parent or ancestor ought to have made, their circumstances, capacities, and mode of bringing up being considered." He desired the abolition of intestate succession to direct heirs as well as collateral heirs. This argument need not be dubbed socialistic. There is much force in favour of the theory. The premises of diffusion theory are that the present system of inequality can be adjusted to bring out an equitable distribution of income and property by taking recourse to taxation as a social measure.

The death duties serve to reduce the inequality of wealth and check the growth of the hereditary plutocracy. Shultz remarks: "A specific proposal to utilize the federal estate duty to check the transfer of family fortunes from generation to generation has occasionally received considerable favourable attention. Under this plan, the estate of every decedent would be divided into two parts—the first part would equal in value the amount of the pro-

† J. A. Hobson: The Coming Taxation (Contemporary Review,) Vol. C-VIII, p. 291.

perty which the decedent inherited and received as gifts during his lifetime, the second would consist of the additional wealth he accumulated through his own efforts. Normal estate tax rates would apply only to this second part of the decedent's estate. An additional discriminatory tax would be levied on the first part. Certain features which recommend this project are lacking in other proposals to use death taxes as a means of equalizing wealth distribution. It is in harmony with the popular disapproval of the 'idle rich.' It cannot be charged with discouraging individual initiative. In this respect, its effect, if any, would be to stimulate increased efforts on the part of rich men, who had inherited their fortunes, to accumulate fortunes of their own to transfer to their children at the lower schedule of rates. Its principle could be effected, without altering the death tax revenue, by simultaneously reducing the death tax rates on earned wealth while increasing the rates on unearned wealth."* The instrument of death duties can be utilized to curb inequalities.

Relation of Death Duties to Income Tax:

One of the arguments in favour of death duties is that it serves as a corrective to unequal distribution and that they would be adequately complementary to income-taxes. As a corrective to uneven distribution, the tax on estates appeals to many as it is based on ability to pay and on the acquisition of "windfall wealth" by the inheritor of property. An inheritance tax will probably be paid by realization of securities, while an income tax will be paid out of the money that would otherwise be saved. The effects of the expectation to pay income-tax each year would be worse than the remoter possibility of one's heirs having to pay inheritance tax at some uncertain future date. In defence of death duties, it has been argued, that the distribution by taxation on inheritances would correct the present inequalities of income and property and would root out inequalities in years to come.

* Shultz: American Public Finance, p. 492.

Income tax has certain definite limitations, the chief of them being that it fails to reach accumulation of a person's wealth which may not fall within the purview of income in the strictest legal sense,* because of the fact that the decedent might have been the recipient of a fortuitous gain or he might be invested with the idea of capital accumulation rather than with the object of immediate profits. In such cases, the income tax, usually falling on the current income of the individual, does not fall upon that form of property the value of which might have suddenly shot up due to several extraneous causes. Death duties therefore can be so administered as to remedy these defects.

There are several other forms of property such as stocks and shares, jewellery, or other durable form of wealth, which may not fall within the purview of income-tax. "A man may invest a sum of money in stocks and shares, or he may spend it on jewellery or other durable form of wealth. Possibly, he would have reason that the enjoyment he (or more likely his wife) receives from the ownership and display of the gems is equivalent to the money interest that could have been obtained from an ordinary investment. Possibly, too, he would argue that there is a likelihood of the jewels appreciating in value, in which case the investment analogy would be even closer. Yet the material income from these possessions would be immune from taxation. The imposition of death duties, on the passing of this wealth does not redress this inequality in taxation during lifetime, but, at least it prevents it from being perpetuated." † Death duties can be justified on grounds of ability and they do not affect production and saving when taxes on wealth yielding 'psychic' income are levied.

Another way in which death duties can serve as a complementary force in rectifying the deficiencies of income-tax is by way of pursuing differentiation between earned and invested incomes. Although income tax does

* Silverman: Taxation, Its Incidence & Effects, p. 183.
† Ibid, p. 185-6.

take into consideration differentiation between earned and unearned incomes, the real differentiation in favour of earned incomes is actually greater than the nominal proportion. When income tax thus suffers from deficiency imposing of death duties is substantially justified in rectifying and correcting the mal-adjustments in income-taxation.

Theories Against Death Duties:

In opposition to levying of death duties, several theories have been propounded:

Natural Right Theory:

It is said that death duties give affront to the natural right of the individual to possess property and his or her natural right of inheritance and bequest.† The right of inheritance to the property of the decedent is quite natural one inasmuch as the successor has blood relationship with the decedent. But in modern times, it is argued, that all the rights belong to the State and that the prevalence of the rights should be in accordance with the best interests of the society at large. Though supposing that inheritance has been considered as a natural right (as is held by the Supreme Court of Wisconsin), it does not impose any limitations on the part of the State to pursue a system of death duties. Inheritance is a well-established characteristic of the institution of private property and has been criticised much as affording the capitalist a greater power to suppress the labourers. No modern Government could ever think of giving such a free hand to private owners so as to enable them to be responsible for the steep gradation of incomes. Almost all these sentiments have been echoed in the writings of Jeremy Bentham and J. S. Mill, wherein they questioned the right of inheritance. In fact, the former went so far as to advocate a complete abolition of inheritance in the case of direct heirs. To him, there was never anything as a natural right of inheritance, and that the extension of intestate

† Shultz; The Taxation of Inheritance, p. 169.

succession to collateral relatives was under existing social conditions defensible only to a very limited extent. Dr. West said: "Bentham's plan was to abolish intestate inheritance except between immediate relatives, to restrict the power of bequest of testators having no direct heirs, and to give the state a part of the property of decedents in certain cases. He called the system which he proposed an extension of escheat, and based it not upon any right of inheritance in the state, but upon the absence of any reason for the operation of intestate inheritance between individuals not closely related." On the other hand, Mill advocated a serious limitation of the inherited property. He wrote: "Inequalities of property which arise from unequal industry, frugality, perseverance, talent and, to a certain extent, even opportunities, are inseparable from the principle of private property and we accept the principle that we must bear with these consequences of it; but I see nothing objectionable in fixing a limit to what anyone may acquire by the mere favour of others, without any exercise of his faculties and in requiring that if he desires any further accession of fortune, he shall work for it."* Thus, he argues for a limitation of the property that has been inherited by the beneficiary from the decedent. The orthodox school of economists never lacked enthusiasm to declare that the possession of property and its transmission at death were natural rights and that they should be recognized by the public authority. The institution of private property is said to be so essential in the best interests of society that "if it did not exist it would be necessary to invent it. All death duties weaken this institution of property and inheritance."

Death Duties and Capital :

It was a common argument in the 19th century that taxes on capital values—property and inheritance taxes—actually destroyed capital. It is still being repeated by some. Capital has been defined as "the 'tool fund' of society; that is, the income which has been set aside for

* J. S. Mill: Principles of Political Economy.

investment in machinery, buildings, and other productive assets plus those already in existence." † Any form of death duties paid out of capital result in the breaking up or the destruction of capital that has already been accumulated. The argument has been explained in a general way as follows: "Any tax measured by capital reduces capital; the death tax is measured by capital; therefore it reduces capital." Grave is the error here. Death taxes are not generally paid out of capital. All taxes, even those based upon the capital value, are paid out of current income or income not yet converted into capital plant.†† Even the property tax might be paid out of the income that the tax-payer might have obtained from other sources or out of the income yielded by the taxed property itself. Similarly, a death duty or a capital levy might be paid out of the proceeds of the sale of the property, or from the amount saved. This might result in "dis-saving" and to that extent death duties might have to be responsible for the dissipation of the capital already accumulated. As we have previously seen, dissipation of capital might even be due to a highly progressive tax. The income-tax payer might be compelled under certain circumstances to sell away a part of his property, to pay his income-tax. If the general property tax and death duties fall upon the capital so as to destroy it to that extent the same argument holds good in the case of income-tax. Though income-tax is expected to fall on the current income of the individual, it might so happen that the recipient finding his income too little, might be compelled to withdraw a part of the money from either his savings or by selling away a part of his property.

Nevertheless, the effect of death duties on national capital are bound to prove, to some extent, adverse due to the abrupt transmission of capital in the form of property from the decedent to the inheritor. "Forced sale of assets may break the family control of a business, put-

† H. M. Groves: Financing Government, 232.

†† Shultz; American Public Finance, p. 269.

ting control in the hands of others who may not have the same interest or ability to carry on the business. Business may thus deteriorate and the capital be diminished or destroyed. Carried to the extreme, death taxes may be so heavy, especially if other taxation were also heavy, that it would be impossible to find purchasers for the capital formerly in the hands of private enterprise. Even this would not mean the immediate destruction of capital; but there is no reason to suspect that under Government ownership, the capital would not be so wisely or efficiently employed and that deterioration and loss of capital might result. Incidentally, this brings us to the social motive. There, doubtless, are some who would favour using the death taxes for precisely this purpose, i.e. as a means of expropriating privately-owned capital." * As a general argument, it has been adduced that most of the taxes are met out of potential savings, except in those cases where the individuals, either due to force of habit or due to lack of means, will be compelled to draw out from the savings "Estate taxation, as any tax on capital, has the peculiar advantage in that a complete offset of losses is automatically assured. This arises from the fact that an investment loss is also a capital loss and thus directly reduces the future estate tax liability. The presence of taxable income, against which a loss may be offset, is not required. This is an important reason why estate tax rates are less likely to interfere with investment incentives than equivalent sur-tax rates under the personal income-tax." †

Granted that the death duties, or to be more specific, estate duty may have to be paid out of the particular estate, "from the collective point of view, however, there will be no loss of existing capital, for ultimately the source of payment will be somebody's income. The executors may have to sell securities in order to find the necessary lump sum. The immediate purchaser may take up those

* "A Tax Programme for Solvent America" by the Committee on Post-war Policy published in 1945.

† Public Finance and Full Employment, Post-war Economic Studies, No. III, December, 1945.

securities with the proceeds of some sale which he in turn has effected; there may, in fact, be a chain of transactions amounting to no more than a transfer of existing capital. But the chain must lead eventually to a purchaser who has savings out of income to dispose of; it is those savings out of income which ultimately provide for payment of the duty."†† Thus the death duties do not destroy the existing capital as they are not paid out of capital, and as such any argument that will be advanced to the effect that the government lives upon its capital, is misleading. Death duties only divert the capital into different channels, and thus prevent new capital from entering the originally intended avenues. The Minority Report of the Colwyn Committee remarks: "Though death duties are assessed on capital they destroy no existing capital; at most they absorb potential capital by diverting to the payment of the duties, income which would otherwise have gone into new savings. In this they do not differ from Income Tax or any other tax of comparable magnitude. The property sold must eventually be bought by someone who has free income seeking an investment, and the only effect is to divert this income from the creation of a new, to the purchase of an existing, investment. There is no reduction of actual capital." *

At most, it can be regarded as a capital levy. We quote Sir S. Holmes who remarked that: "We have had a capital levy in this country since the days of Sir Harcourt, namely, Death Duties. In my opinion, that sort of capital levy is the only one which would not cause chaos in the country, for the very obvious reason that when a man dies the Death Duties have to be paid on his estate, the requisite amount on his estate has to be realised, and the rest of the community are able to buy his shares, chattles, or whatever it may be. Therefore, the executors are able to dispose of the necessary amount of his property, and the Chancellor gets a form of capital levy. But if there is to be a capital levy for everybody at

†† Majority Report of the Colwyn Committee, Para 514.
* Minority Report of the Colwyn Committee, Para 253.

the same time, then everybody would be a seller and there would be no buyers, resulting in absolute chaos. It would throw the country into a state of chaos, which would ruin production and cause unemployment. It is a completely impracticable proposal". †

Death Duties and Saving:

Death duties fall upon the aggregate savings within a country. This was one of the several arguments put forth by the British businessmen and capitalists when in 1894 the estate duty was being discussed in England. Although they do not help savings as they strike the potential savings, death duties stimulate the propensity to work and to save on the part of the successors. Prof. Pigou in his evidence before the Colwyn Committee, was against the theory that death duties have deterrent effects, and said that they "are rather a good form of taxation, in that people are probably not discouraged from saving by thinking of the death duties as they are by thinking of an Income tax on unearned incomes". Dr. Dalton in his evidence said that "the prospect of heavy death duties will stimulate those who are waiting for a windfall of inherited wealth to work harder and to save more than they would otherwise do". The death of the decedent naturally means the participation of the state in the sharing of the property of the deceased and this gives room for the successors to put in more labour and earn for themselves rather than to depend on the decedent.

General Arguments Against Death Duties:

Some vague arguments are raised against death duties. Generally, the rates of the duties are arbitrary because it will be difficult to make them correspond to the canon of ability. To add to that, if the same estate is taxed over and over again, there is every possibility for the total disappearance of the estate. The productivity of the tax also depends upon the number of times the estate passes hands in one generation. The greater

† Parliamentary Debates (Hansard) 7th April 1948.

the number of times it passes, the more unjust the tax will be. The common experience has been that quick succession is an exception rather than the rule. But where it is the rule, death duties will certainly be unjust. If, on the other hand, the rapidity of succession or the varying frequency of deaths is slow, it may be that the requisite revenue may not be collected. Bentham argues that "a Chancellor of the Exchequer cannot estimate the yield at all accurately for he does not know which rich men will die during the coming year. Over, say, fifty years, one estate may not change hands at all and so may yield nothing in death duties, while another may change hands several times." Those difficulties can be surmounted by the public authorities provided they are meticulous in following a safe exemption limit, and provided the rate of progression pursued compares favourably with the marginal utility of incomes.

It has been the other accusation against death duties that in so far as they culminate in the breaking up of the large estates, they might destroy an effective combination of business capital and direction.* This argument could be valid under those conditions when land bulked the most important part of property, but as its importance dwindled, much of its force was lost.

It should be concluded that despite the several objections that are advanced against the death duties, it needs must be emphatically said that they have proved to be a good source of revenue, and in as far as they fall upon those recipients whose ability is great, they are just and equitable. In modern times, the governments are relying more and more upon this source of revenue, which has been dependable and substantial.

* Groves: Financing Government, p. 235.

CHAPTER 5.

Structure of Death Duties

1. Progression in Rates. 2. Minimum Exemption. 3. Graduation—Consanguinity of the Heir or Relationship Discrimination. 4. Rignano's Scheme of Death Duties. 5. Variant of Rignano's Proposals by Dalton — U.K. — U.S.A. — Australia — Canada —Summary.

Progression in Rates:

Progression can be more than justified in the case of death duties wherein unearned increment or windfall wealth is taxed. According to the 'benefit' theory, the state is supposed to accord greater protection to the richer rather than to the poorer inheritor, so as to prevent the former from being robbed. From the 'service' theory, the services of the state to the rich inheritors in the safeguarding of their interests can justify any progression in death duties. Progression can be based in conformity with the ability or the faculty of the individual inheritor. "Equality of sacrifice" is a companion of "ability" and lends colour to the argument of progression. As the marginal utility of the incomes of the rich inheritors is lower than that of the poor, progression can be made to correspond to the ability of the respective beneficiaries. If, however, the rich and the poor inheritors are taxed proportionately, the imposition of the duty will be justifiable. While proportionally equal deductions from the larger and smaller inheritances are wholly unjust, a relatively larger deduction should be made from the larger inheritances rather than the smaller. Then alone can equality of sacrifice be achieved.

Another consideration in defence of progression in the rates of death duties is that the relative taxable capacities of the inheritors cannot be determined by the value

of the inherited property and their economic status. Wealth is not a helpful basis in the matter of taxation. The share of an estate received by a beneficiary does not alone constitute the wealth. His economic position before receiving the share should also be considered in introducing progression. It is therefore fully justifiable that the richer inheritors should be taxed progressively than the poorer.

A compensatory argument is put forward in favour of progressive taxation. As variations in the amount of property inherited by different individuals can be attributed to some extent to acts of omission and commission by the state, progressive taxation on the unearned increment is justified. The compensation, therefore, is from the point of the services and obligations discharged by the state. A tax is progressive not because some property has to be given by way of compensation; not because of the services rendered by the state; not also because of the benefit that the individual inheritors obtained from the state; but mainly because of the ability of the individual inheritor to pay the progressive tax, and the social intent of the state.

The state imbued with the social intent of 'equal distribution' of the wealth in the process of transmission of property, uses the occasion of death adjusting unequal distribution of wealth and income. With the social intention to equalize distribution of wealth and putting an end thereby to the undesirable effects of hereditary transmissions of property, any scheme of progression can be justified.

Progressive taxation is advocated as an engine of social improvement, and Adolph Wagner advocated progressive taxation as a means of equalizing the distribution of wealth and income and advancing the nationalization of industry. As Buehler says, the socialists and other reformers have long eyed death duties as preventives for the transmission of great fortunes from one generation to another. The socialist writers take the extreme view that progressive death duties should be introduced to bring about a wholesale socialization. But others, like Marx, think that even highly progressive death duties

might be only palliatives for bringing about equal distribution of property.

Death duties, when they conform to a steep rate of progression, can yield more than when they are imposed on the proportional basis. A progressive death duty will produce greater revenue than a proportional one unless the rates in the latter case are raised so high as to become almost unbearable. But taken individually, the progressive estate duty which imposes a heavier burden than an inheritance tax, is highly productive than the latter; the former takes into consideration only the aggregate value and not the individual shares of the beneficiaries. Progression from one intent or another of the state should be strictly followed in the fixation of the rates of death duties. "The only important tax to which the progressive scale is at all applicable at present is the inheritance tax." *

Progressive rates can be based either on totality or by brackets. In the former case, the taxes will be progressive according to the totality of the estate or the share, whereby the successive rates of the schedule apply to the entire estate or to the particular share. In the latter case, progression in death duties can be administered by brackets whereby the rate of each bracket applies to only a part of the estate or the share that falls within the compass of the bracket. Progression in the former case is older than progression in the latter. The Federal Inheritance Tax (1898) in the case of the United States of America was progressive by totality. That means transfers in the direct line, say in an offer, $25,000 were taxable at three fourths of 1% on the excess of the general exemption of $10,000; if the amount exceeded $25,000 but not $100,000, the entire excess over $10,000 was taxable at 1¼th, and so on. This is the feature of progression by totality. This principle was disapproved by the Supreme Court in the United States, though it had otherwise brought about the taxes. At present, the Federal Estate Taxes and the estate inheritance tax are progressive by

* Seligman: Progressive Taxation, p. 324.

brackets. That means those inheritances which range between $50,000 and $100,000 bracket will have to pay a tax say 2%. The principal difference is that, according to the parallel rates, a tax progressive by totality will yield much more revenue than one progressive by brackets. * This is a great virtue in the case of progression by totality as the tax produces greater revenue than a similar tax which is progressive by brackets. Once the tax is progressive according to totality, the upper schedule of the rates will be applicable to the whole mass of estates or shares whereas when it is progressive by brackets, only limited fractions of an estate or a share of it will be progressively taxed.

The other most important issues in Death Duties, as in the field of taxation, as a whole, are the minimum exemption and the graduation.

Minimum Exemption:

The public authorities have in recent times been following a systematic exemption policy in taxation, and "exemptions have tended to increase as various groups have sought complete or partial escape from the rising tide of taxation. Fundamentally, there are three valid reasons for tax exemptions: (1) that the productivity of a tax will be increased in the long run; (2) that a more equitable distribution of taxation will result and thereby promote desirable social objectives; and (3) that a certain activity of private institutions is of such vast public importance that, like the public schools, it should not be burdened with taxation." † The principle of exemption in income taxation bears testimony to the fact that those persons with minimum incomes should be exempted from the taxation. The principle of fiscal justice that culminates in a scheme of high exemption can be pursued for good in the field of death duties also.

Minimum exemptions in death duties can be treated as personal exemptions i.e. the beneficiaries

* Jensen; Government Finance, p. 407.

† Buehler; Public Finance, p. 431.

of the heir will be enabled to enjoy personally the exemption as a result of the blood-relationship that they bear with the decedent. Exemptions are classified under three heads: conditional, continuous and vanishing. The first form of exemption is a *conditional* one as the amount is exempted only if the prescribed limit is not crossed. If the total value of property inherited by the heir from the decedent is more than the exemption limit, the whole of the property would be fully taxed. If the beneficiary is allowed an exemption of Rs. 50,000 and if he has only inherited property worth Rs. 50,000, he will be fully exempt from death duties. But, on the other hand, if the value of the property inherited is even a rupee more than the prescribed limit, death duties will be levied on the aggregate value of the property inherited without any consideration of the exemption limit. This system is prevalent in almost all the Australian provinces and many European countries. This form of exemptions seems objectionable as the limit of exemption, when crossed even to the slightest degree, introduces arbitrariness and injustice in the rate of the tax. The proper course would have been that when the exemption limit is placed on property, the inheritor should be given the concession to the extent of the level of the exemption. The second form of exemption which is of the *'continuous'* type, fully embodies this principle that even if once the exempted limit has been crossed, only the value of the property which is over and above the limit would be taxed. What has been found to be unjustifiable in the former case has been more than compensated in the latter, and no kind of hardship is placed upon that heir who might have by sheer ill-luck inherited property, the value of which is just above the limit of exemption. The third and the most reliable form of exemption is of the *'vanishing'* type according to which any increase in the value of the property inherited from the decedent will be taxed in a diminishing proportion, with the result that a point will be reached when the whole of exemption might vanish. "That is, a specified amount, say $500, which, if it constitutes

the whole of the net value of the share, remains untaxed; but if the net value exceed $500, the exemption diminishes in accord with a prescribed scale, until it reaches the vanishing point—for example, if the exemption diminishes $1 for every $1 by which the value exceeds $500, then if the total value were $750, the exemption would be $250 and the taxable amount $500; but if the value were $1,000 (which in that case would be the vanishing point), the whole amount would be taxable."* Thus, the greatest advantage in the vanishing form of exemption will be the assurance of substantial justice to the beneficiary. It has not received the attention it richly deserves. It is advisable to levy it in the case of those descendants who bear blood relationship with the decedent. It will be highly productive if the vast amounts of inherited property transferred to direct heirs are taxed on the basis of the vanishing type.

Minimum exemptions are justified in the case of those inheritors who are greatly affected by the loss of the property of their family. The sacrifice that individual beneficiaries make in the payment of death duties depends upon the expectedness or otherwise of the inheritance and the nearness of their relationship with the decedent. The size of exemption that each beneficiary enjoys is often determined by the consanguinity of the heir. It should however be made clear that in the case of the surviving spouse and minor children, who have lost their sole provider and to whom the inherited property provides the only basis of their existence, any tax without sufficient exemption limit, would be an unjust imposition. That is the reason why differentiation is made in the case of the surviving widow or minor children on the one hand, and the brother, nephew, an uncle or a cousin, on the other. In the former case, the inherited property accrued to them as a natural right, and in the accumulation of the property during the lifetime of the decedent, his wife as a joint partner must have contributed her might;

* Australian Royal Commission on Taxation, Fifth Report, p. 234.

whereas in the latter case, neither was the property that has been inherited the result of their exertions nor did they come to possess property after having anticipated to receive it. Thus, in the former case, any unjust imposition of the Death Duty would diminish to a great extent the survivers' financial capacity owing to the death of their sole provider, while in the latter case, their financial status would not at all be affected.

Minimum exemption from the administrative point of view of Death Duties is quite defensible. If every estate were to be taxed, irrespective of its value, it would be vexatious for collection and it would be yielding less revenue. "Primary intent of the exemption is to save the tax administration the costs of checking and auditing thousands of returns on small estates the tax receipts on which would not cover, or would do little more than cover, the costs involved." Moreover, it has been the experience of many countries in the world that if the minimum exemption is kept at a sufficiently high level, the revenue-yielding capacity of the duty is great. The main consideration that weighed in the matter of raising the exemption limit from £100 to £2,000 in 1946 in U.K. was that as many as 150,000 out of 200,000 estates which were previously liable, ceased to pay estate duty. The result was that the cost of the exchequer was only £2 million compared with the total yield of estate duty which was over £100 million. The new exemption limit relieved the exchequer of bothersome and costly inquiries and investigations into a large number of small estates. It was estimated that out of the 50,000 estates, which would be still liable for, more than 30,000 would have their liability reduced, and the imposition on some 7,000 would remain unaltered. The total yield, despite the exemptions and reductions went up to nearly £22 million.

Graduation:

Graduation of Death Duties is based upon any of the following principles: Firstly, the tax might be graduated according to the value of the property left by the

deceased. Secondly, the tax might be graduated according to the aggregate amount inherited by the individual beneficiaries. Thirdly, it might be in conformity with the wealth that the individual beneficiary has accumulated prior to the inheritance of property of the decedent. Fourthly, it might be in accordance with the consanguinity of the inheritor. Lastly, it might be according to the "age" of the composition of the estate.

According to the first, the tax levied upon the whole of the value of the property, does not take into consideration the distribution of the same amongst several heirs of the decedent. So, following the principle of graduation, relatively heavier duties will be imposed on larger rather than on smaller estates. The British Estate Duty corresponds to this principle. Despite the number of heirs that share the property, the same amount of duty has to be paid according to the schedules. The assumption is that as the tax is imposed upon the property of the deceased, and is ultimately borne by him, the duty be levied according to the value of the property left, rather than by the amount of the individual shares. Though the rates are based on progression, and though they are less susceptible to evasion and avoidance, they do not correspond to the relative abilities of the different beneficiaries. Thus, no consideration is shown to their individual economic status. The argument in favour of them as to the ease in administration of the tax is more than offset by the fixation of the rates without any due recognition of ability, which is one of the most important canons of taxation.

The second principle is the tax would be graduated according to the individual inheritance. If the amount inherited is large, the duty leviable will be highly progressive. This principle "differentiates in favour of a fairly equal distribution among a large number of inheritors, as against a more unequal distribution among a smaller number". Thus the only advantage in adhering to the second principle is that the tax can be fairly distributed amongst the inheritors, though there is also every likelihood for greater arbitrariness in their respective rates. But

all the same, the tax will not differentiate between "earned" and "unearned" wealth, as in the former case. To add to this, in both the above-mentioned principles the economic status of the beneficiaries is not taken into account. The ability of the individual varies with the amount of property inherited as also with the property acquired by himself. Randolph Churchill who did not agree for the taxation of the entire property without any reference to the apportionment or distribution of property, or the consanguinity of the heir, raised a hue and cry in favour of an over-hauling in the field of death duties and argued in defence of a single levy, graduated according to the amount of property inherited by the individual beneficiaries. It was said that owing to administrative difficulties all his plans were foiled and it was only eight years later that Harcourt overhauled the system of death duties, introducing the estate duty and retaining the legacy and succession duties.

The third principle favours the fixation of the rates of Death Duties according to the prior wealth of the beneficiary or heir. It is most equitable that a legatee be taxed on the basis of his ability to pay. It is often argued that since a legatee who has "a larger income than another has to pay a heavier tax on a specific addition to his income, it is just as equitable that the man who already possesses a comparatively larger amount of wealth should bear a greater charge on a specific bequest than one who is not so fortunately situated." That is why critics always point their finger of scorn at cases wherein "a millionaire son inheriting still further millions from his father and paying very low rates on those millions, provides a contrast to the poverty-stricken cousin," who is compelled to surrender the greatest portion of the inherited property to the public authority. Thus, as Shultz remarks, several critics held up to mockery progressive inheritance taxes defended on the doctrine of 'ability,' but which took into account only the size of the inheritance received and not the general financial position

of the heir in determining such 'tax-paying ability.' * This argument has come to receive the earnest attention of several economists who favoured the imposition of taxes by the "continued standard of the size of the inheritance plus the prior wealth of the heir rather than the former alone." This leads to social redistribution of the wealth of the country as a whole and introduces fiscal justice in the realm of taxation. As early as in 1895, the Norwegian Inheritance Tax Law, according to West, made the levy of the tax conditional upon the general economic status of the inheritor, the exemption limit was fixed at a reasonable level by considering together the inheritance and the prior wealth. In Germany, the shares of the surviving spouse and children were exempted when the inherited property plus their previous wealth was less than M. 100,000, and the rate of the tax was increased as the wealth of the beneficiaries increased. In Italy, though the rates underwent changes according to increases in the beneficiaries' wealth, the fractional variations in rates were not witnessed. Instead, additional levies were made.

As Shultz summarises: "Despite the change of discriminating against wealth, this basis of inheritance tax rates upon the 'tax-paying ability' of the beneficiary as measured in part by his prior wealth might be unqualifiedly approved but for one every important practical difficulty. The tax authorities have no effective way of determining, without great expense and trouble and inquisitory searchings, the amount of the prior wealth of the beneficiaries. The suggestion has occasionally been made that his income and property tax reports would provide an index to an individual's wealth, but every tax administrator knows that the margin of error and uncertainty and evasions in these reports are too wide to make them the basis for a further tax determination; there would only be increased incentive to misrepresentation and evasion in these taxes." † No doubt, the difficulty

* Shultz: The Taxation of Inheritance, p. 309.
† Shultz: The Taxation of Inheritance, p. 310-311.

would be great especially when the decedent's property is distributed amongst a number of dependents, but even in those instances, it would not be impossible to arrive at a satisfactory idea of the same on the basis of income-tax returns and property tax reports. In cases, where the real capital property of the individual inheritor is ascertainable, capital can be taken as the criterion, but in all other cases incomes can form a satisfactory index. By adhering to this principle, the tax would be imposed in accordance with the marginal utility of incomes of the individual beneficiary, and it would leave room for adjustment in differentiation between "earned" and "unearned" wealth. All the property inherited can be taken as "unearned" wealth and the property out of personal exertions can be represented as "earned" wealth.

Consanguinity of the Heir or Relationship Discrimination:

One of the significant features in the levy of death duties is the principle of the consanguinity of the heir or relationship discrimination. From the points of view of "back tax" and "service" theories, little justification seems to embody any scheme of relationship discrimination. When the tax is considered as one imposed only because some wealth has escaped taxation previously while the decedent was alive or because of the service of the state in guarding or protecting the property of the inheritor, the principle of blood relationship does not afford any key to the progressivity of death duties. Relationship discrimination in death duties is a highly potential agency in the matter of retention of wealth within the family unit rather than for allowing the aggregate wealth within a community to be widely distributed with this device. Thus, relationship discrimination found great justification in the explanation of the theory of privilege. 'Privilege' can be looked at from two angles; firstly, the family can be considered as one unit and the privilege of the distant relative or descendant of the decedent can justify any imposition of death duties on the principle of relationship discrimination; or secondly, it can be viewed that inheri-

tance is more or less a windfall or a fortuitous gain and that the acquisition of it might justify levying of any duty. This argument carries little weight in the practical fixation of the rates of death duties.

From the point of view of 'ability' or the 'faculty' of the inheritor and, more so, when the descendant bears distant relationship, a highly progressive tax can be levied upon him. Here, it corresponds to the faculty theory which has been applauded by most of the economists of the present century. "Windfall wealth" argument along with the ability theory indicates very great justification in the imposition of any steeply progressive death duties. Gladstone said nearly a century ago that "those who enjoy direct succession are educated in expectation founded on that succession,. are trained up, and have their habits and mode of life formed with relation to the property they look forward to enjoying. Upon them, therefore, it would be a great hardship, were the State to step in and take away any material portion of that property which they have been taught to expect. On the other hand, succession of strangers and of persons not within traceable degress of consanguinity, are successions very commonly of an accidental character and are unconnected with any training or expectations. These are successions too, in relation to which caprice takes a large range. It does appear, therefore, very reasonable that a scale founded on degress of consanguinity should be maintained." The fundamental basis of any scheme of relationship discrimination or the consanguinity of the heir is embodied in the "implications of expectancy and dependency" and in the "universal feeling that to inherit from a parent is not the same thing as to inherit from a brother or sister; that the difference is greater when the inheritance is from an uncle or an aunt, still greater when it is from more distant relatives, and greatest of all when it is from absolute strangers; and nobody finds fault with the legislature for bearing these differences in mind when fixing the rates of death duties." * To add to this, administrative

* Pierson: Vol. II, p. 506.

reasons also justify the pursuit of this discrimination.

There had been a clamour of opinion in favour of exemptions and relationship discrimination in the matter of fixation of the rates of the death duties. It was the sense of family union and the family ownership of property that has invoked such a form of relationship discrimination. The French, the Spanish, the Italian, the German, the English and the American writers have all condemned taxation of the direct heirs and advocated a scheme of exemption and relationship discrimination in their case, allowing the beneficiaries from distant relationship with the decedent to be taxed at a highly progressive rate. The taxing authorities have generally found it more convenient and justifiable to pursue the scheme of exemption and relationship discrimination for beneficiaries who were near and dear to the decedent. Any rate discrimination between the direct and indirect heirs, can be of two kinds: one the *horizontal,* and the other *vertical.* "By the first method, the direct heirs are placed in the first class, brothers and sisters in the second, uncles and aunts and nephews and nieces in the third, and grand-uncles and-aunts, cousins and grand-nephews and-nieces in the fourth, and so on; by the second method the direct heirs are put in the first class, brothers and sisters and their descendants in the second, uncles and aunts and their descendants in the third, grand-uncles and-aunts and their descendants in the fourth, and so on." †

Rignano's Scheme of Death Duties:

"Up to the present, the principle of graduation has been applied to death duties according to two criteria: the size of the estate, and the degree of relationship of the beneficiaries. But there is a third criterian which would admit of graduated rates, and this is the *relative age,* if one may name it thus, of the different portions of the estate left by the deceased—or more exactly, the *number of transfers* in the way of succession and donation which

† Shultz: The Taxation of Inheritance, p. 268.

the different portions of the estate have undergone before coming into the possession of the deceased. By the application of this criterian of *progression in time*, the right of the testator would vary with the different increments of his estate". *

Prof. Rignano in his exquisite book, *Di un Socialismo in Accordo colla Dottrina Economica Liberale,* expatiated on the principle of progressivity 'in time' of inheritance tax. According to it the rate of the tax increases with the number of times that the property subject to it has already passed hands through transmission. Suppose that the tax levied on the first inheritance is one third, on the second it will be two thirds, and on the third, the whole of the property will be taken over by the state. Dr. Dalton has elaborated the same process thus: "Suppose that A, who receives nothing by inheritance, acquires by work and saving property of value *a,* which he leaves by will to B. Then the tax will be 1|3 *a* and B will receive 2|3 *a.* Suppose that B, by his own work and saving, adds a further amount *b* to his inheritance of 2|3 *a*, and leaves the whole by will to C. Then the tax will be, as to the 2|3 *a*, two-thirds and, as to the *b*, one-third. Therefore the total tax will be 4|9 *a* + 1|3 *b* and C will receive 2|9 *a* + 2|3 *b*. Suppose that C, by his own work and saving, adds a further amount *c* to his inheritance and leaves the whole by will to D. Then the tax will be, at to the *c,* one-third. Therefore the total tax will be 2|9 *a* + 4|9*b* + 1|3 *c*, and D will receive 2|9 *b* + 2|3*c*. And so on indefinitely, each person's addition, if any, to his inheritance being wiped out by taxation in the course of three transmissions." †

As Rignano says, "in effect, on the death of the grandson of each accumulator, or more generally of the heir of his immediate heir, the State would have nationalised a third of the personal fortune of the deceased, seven-ninths of that accumulated by his father, and the

* E. Rignano: The Social Significance of Death Duties, Ed. by Sir Josiah Stamp, p. 37-38.

† Dr. Hugh Dalton; Inequality of Incomes, p. 316-17.

whole of that accumulated by his grandfather". † We are indebted to Huet who, in 1852, favoured the idea that, after the second generation, inherited wealth should be acquired by the state on the plea that the right to leave property depended on the testator's ability to produce wealth and, that on other grounds, especially ethical, it was not fair that wealth not earned by the testator himself should be allowed to descend upon him. According to him therefore, after the second generation, the estate should ultimately go in full to the state. Thus, the right to transmit wealth by testament depended on the distinct quality of producer or creator of that wealth, on the basis of which Huet advocated for the full acquisition by the state of the inherited property. This was the principle that underlay the scheme of Rignano. Socialist as he was, his primary intention was to utilise death duties as a means by which equality could be restored by redistributing the incomes. Rignano did not attach as much ethical importance as Huet did. To him the economic argument was more formidable. Rignano in his plan made it clear that "the sole way to achieve the effective and gradual nationalization of private capital without injuring the delicate mechanism of economic production" lay in utilizing the instrument of death duties. According to him, the whole of the estate was divided into two categories: first, that part of the estate inherited or received by way of bequest, and secondly, the wealth accumulated by the testator as a result of his own efforts during his lifetime.

The plan seeks to differentiate between wealth due to the effort of saving of the testator and the wealth which he received by way of inheritance or gift. "Once the estate of the testator was thus quantitatively divided, the nation would not levy on the portion due to his labour a higher tax than it imposes to-day. On the portion which the deceased inherited directly from his father, the nation would make a heavier levy, say 50%. On the portion which came to him from his grandfather, through

† Social Significance of Death Duties, p. 47.

the medium of his father, there would be levied a very heavy tax, possibly 100%." * Thus, while a lower rate would be imposed on that part of the estate due to the acquisition of the testator himself, a higher rate will be collected from that portion of the property which has been inherited by the testator. The main idea underlying the Rignano's scheme is that most of the testators concentrate their attention only on their immediate heirs rather than on their distant ones.

One of Rignano's schemes has been critically viewed by well-known writers. It comprises a "Maximum Project" and a "Minimum Project." Both aim at the transference of land and industrial capital to the control of the state or public controlled organizations but the former is the more drastic of the two as a socialistic instrument. The novel features are firstly, it draws a line between the part of a man's estate which he himself has accumulated and the portion which has come down to him from his benefactors. Death duties discriminate in favour of the former. Secondly, the idea is that taxation should be graduated according to the number of times that the inherited property has passed on until eventually the tax becomes 100% of the estate received. Under this project, an estate is divided into three parts: that which the deceased did not inherit, the portion which he received from his immediate predecessors and lastly the part which passed down to him from two generations back. On the first portion there would be no higher tax than that at present. On the second portion the tax would be 50% of the value of the estate and on the third portion, a 100%. The scheme intends to prevent an estate from passing beyond the third generation.

The minimum project would divide the estate into two parts, against the three under the former—the "earned" and the "inherited." The scheme provides for death duty at the existing rates on the "earned" portion of the inheritance and at double the rate on the "inherited" portion. Thus under the 'maximum' project,

* The Social Significance of Death Duties, p. 38-39.

the percentage deducted from an estate would increase at each time of transmission until within two or three generations the whole of the estate would be appropriated and under the 'minimum' project, a lower rate of duty is to be levied on the part of estate due to the savings of the decedent and a higher rate on that part which he might have inherited. Under the 'maximum' project, there seems to be therefore, a great chance for socialization at the earliest time, and almost all the extreme socialists argued in favour of it.

Under this scheme, no account would be taken of the history of the property during the lifetime of the heir and the savings of the heir would only be measured by the full amount of the excess of his net estate at death over what he might have received by way of inheritance or gift. That means "if someone has inherited £60,000, if he dissipates this and later accumulates £100,000, the nation has no alternative but to consider the first £60,000 as representing the inherited property." * Rignano's proposal, therefore, is that in addition to graduation of estate duty in accordance with the size of the estate of the deceased, the rates of the duty might be differentiated according to the "relative age" of the estate, that is to say, the number of times the property of the decedent has been the subject of inheritance and bequest. If a person dies leaving £100,000, of which £50,000 was acquired by himself, the remaining £50,000 which had been inherited by him can be taxed heavily.

This proposal has been elaborately dealt with by the Minority Report of the Colwyn Committee. The proposal, it says, distinguishes three rates of duties, running up to 100% in the case of the third transfer, so that the whole balance of an estate would pass on to the state. The following is an illustration given in the Minority Report to show the functioning of this plan. It is assumed that the rates were 30% on the first, 60% on the second, and 100% on the third transfers :

* The Social Significance of Death Duties, p. 70-71.

A inherits nothing and accumulates from his own business &c., £100,000.

First Transfer

On A's death the state takes duty at 30% (i.e. £30,000), leaving £70,000 to be inherited by B.

B increases this by his savings to £200,000.

Second Transfer

On B's death the state takes duty at 60 per cent. on £70,000 (i.e. £42,000) and at 30 per cent. on £130,000 (i.e. £39,000) = Total £81,000.

Third Transfer

At C's death the state takes duty

at 100% on £ 28,000	...	(i.e. £28,000)
at 60% on £ 91,000	...	(i.e. £54,600)
at 30% on £131,000	..	(i.e. £39,300)
		£121,900

The original £100,000 is thus reduced by £30,000 to £70,000 at the first transfer, by £42,000 to £28,000 at the second transfer and by £28,000 to nil at the third transfer.

According to the Minority Report, a simpler method can be evolved out of this by following only two rates of duty: one applicable to all wealth received by inheritance or gifts, whatever its relative age, and the other to that portion of the estate accumulated by the deceased as a result of his exertions during his lifetime. Assuming these two rates to be 60% and 30%, according to the Minority Report, the above case would work out as follows:

On A's death, the state takes duty		
at 30% on £100,000		
On B's death, the state takes duty		
at 60% on £ 70,000	..	£ 42,000
at 30% on £130,000	..	£39,000
		£ 81,000
On C's death, the state takes duty		
at 60% on £119,000	..	£ 71,400
at 30% on £131,000	..	£ 39,300
		£110,700

1. *Practicability*: Several administrative difficulties have been mentioned. "This tracing of gifts would be particularly difficult and, even with special provisions and with drastic penalties for concealment, the incentive to, and the opportunities for, evasion would be considerable. Even if in all the conditions required, a scheme could be worked practically in this country—which is 'perhaps doubtful'—it 'could not in its initial stages be fully and effectively administered, so as to secure a correct assessment and equality as between one tax payer and another. Probably it would only be after the taxation had been in operation for a considerable period, say, two generations, and full and elaborate records had been accumulated that it could be anticipated that the administration of the tax would approximate to the standard prevailing in the case of the other main direct taxes". * If only two rates were to be followed, as the Minority Report has emphasised, individual injustice could be removed to a great extent. Moreover, it may not be found impracticable to differentiate between that portion of the estate that had formed the inherited property and the portion which had been acquired through the testator's own exertions. Introducing two rates of death duties and by dividing the whole estate

* Colwyn Committee, p. 314.

into two parts, one equal in value to the balance, would be convenient to the tax-payers as well as to the administration. † But still, as the Board of Inland Revenue has pointed out "it would not be impracticable to introduce in the country an effective scheme of death duty taxation on the lines of the Rignano's principle", by making special provisions for dealing with the joint investments and settlements; trusts and gifts *inter vivos*. Apart from all this, the cost of the project is another problem which, if only could correspond to the rate structure that has been evolved by the Minority Report, would be relatively less.

2. *Equity*: On grounds of equity, strong criticism is advanced against Rignano's project. It might so happen that, while transmission of property takes place from the first to the second generation, the purchasing power of money might vary. Any decrease in it would naturally cause a fluctuation in the real value of the property. It would be a great injustice if the rate structure did not take into consideration the major fluctuations in the purchasing power. "If the savings of the testator were to be measured simply by taking the excess of the net value of his property at death over the net value of what he had received by gift or bequest in the course of his life, without any allowance for appreciation or depreciation of the property so received, glaring inequalities would be found to result. Some of these might, no doubt, be modified. Prof. Rignano himself recognises that it might be necessary to provide for alterations in the general value of money by a system of index numbers". * But fluctuations in the purchasing power of money form only one aspect of the whole problem. As the inheritor receives property and stocks and shares etc., the value of which may fluctuate from day to day, the preparation of index numbers can be in conformity with the rate structure.

Prof. Rignano is of the opinion that "it would always be possible to introduce statutory exceptions for cases

† Silverman: Taxation, Its Incidence and Effects, p. 214.

* Colwyn Committee Report, p. 314-315.

where the inherited estate might be lost through fortuitous circumstances or *force majeure*." "However," he adds: "a competent tribunal would have to pass upon such cases, and closely check and limit them, in order that the entire significance of the reform should not be lost." * But this would introduce on of the greatest problems and from the point of view of administration too, it would be extremely difficult to think of satisfying all the inheritors who apply for statutory relief and for extra statutory exemptions and concessions. The difficulty will be all the more greater in the maximum project.

3. *Effects on Savings:* The main idea underlying the Rignano scheme of death duties is that a person regards the wealth that has been accumulated due to his own efforts "as having a greater value than an equivalent sum which he had inherited". This is how discrimination could be adhered to in the matter of taxing highly the portion of property that had been acquired by the inheritor himself, leaving inherited property to be taxed more heavily. "It is this extra value, so to speak, inherent in the wealth accumulated by his own labour and thrift, that would provide the heir with a new incentive to labour and economise, three or four times greater than the present stimulus". It is quite difficult to point out whether there is stimulus at all, particularly when a tax is levied so as to take away the property within one or two generations. On the other hand, it has been one of the main arguments against death duties that it would reduce considerably the incentive to work and save. The differentiation between earned and unearned incomes which is being followed in the case of income taxation can be pursued in the case of death duties too, inasmuch as earned wealth can be more lightly taxed than the unearned wealth, and surely the effects on the incentive to work and to save will be less harmful to business enterprise and economic initiative, when graduation is based on that differentiation. Prof. Rignano was very much confident that his scheme would increase the incentive to work as well as to save, since

* Social Significance of Death Duties, p. 91

"as regards one's own children, every sum saved by the heir of a given estate, would come to have, in his eyes, a much greater value, even three or four times greater, than the sum he had himself inherited." * The Colwyn Committee in its examination of the Rignano proposal was more inclined to consider it from the point of the tax payer. Without his willing acceptance or the co-operation, an adverse effect on savings might be witnessed. "An owner of inherited property which was threatened with a high rate of duty or with extinction on his death would very often be impelled to work and save; in the normal case the comparatively low-rate of his own savings would be a considerable incentive, and the prospect that those savings in their turn would suffer a heavier rate on the death of his heir would not be seriously repressive. On the other hand, the owner of inherited property might be drawn to speculative investment, since capital accumulated by speculation would be taxed at the lower rate just as much as any other savings; again, he might be strongly tempted to evade paying the duty, especially by means of making gifts which would be very hard to check; finally, he might be induced to squander the capital, if his children or other prospective beneficiaries were already flourishing on their own. It is arguable, however, that, if the scheme could be introduced in a form commending it to the tax payer, it would exercise a beneficial influence on work and saving. Any immediate effect in this direction might be increased if the higher rates at the second or the third transmission enabled lower rates than those now existing to be charged on the first transmission". †

Variant of Rignano's proposals by Dalton:

Dalton sponsored a variant to the proposal to modify the Rignano scheme. Having thought that the Rignano scheme might eventually result in extravagant expenditure on the part of the inheritor as well as increased gifts

* The Social Significance of Death Duties; p. 39.

† Colwyn Committee Report, p. 316.

inter vivos, he proposed to check these defects by imposing on the net amount of the wealth inherited, after the usual taxes have been paid, a supplementary tax at a fixed rate, and the charge was to be payable in either cash or government securities or other approved securities or in any other form to be agreed upon. That charge, as if it were, based upon mortgaging an estate, transmitted from the decedent to the beneficiary, indicates an additional amount representing the liability at the next passing. Thus, over and above the usual death duties, to be levied on the property inherited, a supplementary duty will also be levied, equal to the amount earmarked for appropriation at the next change of ownership. * In return for this supplementary levy, the inheritor would receive from the public authority a terminable annuity, based upon the annual value of the securities etc. on the day when they were to be paid over to the state. Under this proposal the estate does not directly bear the burden to pay the beneficiary. The estate itself is left in the hands of a Public Trustee, only the income from it being paid to the beneficiaries. Personal possessions, capital in private business and shares in highly speculative concerns are exempt from this treatment. The proposal has a merit of saving property from actual alienation. Certain portion of each estate or inheritance representing the special deferred tax on inherited property is to be handed over to the state on the first passing of the property and converted into an annuity giving the same income as before but terminable on the death of the first beneficiary or after a certain fixed numbers of years.

Another adaption has also been suggested. It is proposed firstly that the proportion of each estate absorbed by the increase in duty could be handed over to the state within broad categories of assets—not in cash but in the form in which it existed at the time and secondly that the estate should receive in exchange annuities, say, for 20 years with an annual value equal to the income from the

* C. F. Silverman: The Tax, Its effects and Incidence, p. 219.

proportion of the estate transferred. This annuity might be for a fixed number of years or might run till the death of the beneficiary, with the result that "so far as the immediate income was concerned, the inheritor would not lose anything, but there would be a time-limit set. They would be holding a wasting asset in place of a permanent source of income".

It is quite certain that the treasury will eventually obtain the whole of the capital sum without any fear of it being dissipated by the inheritor, as in the Rignano scheme. Thus, under the variant on Rignano's scheme suggested by Dalton that contingency can be avoided. The individual inheritor is reassured of the annuity for either a fixed number of years or till his death and, to that extent, he would be in a position to co-operate with the taxing authority. There is also the incentive to save.

Dalton is of opinion that the supplementary levy would surely be beneficial and fill the gap in the Rignano scheme. He also claims that inheritors "would be stimulated by the prospect of the annuities running out, to work and save in order to make good the prospective loss of income". Serious objections have been expressed over Dalton's views. They are embodied in the Colwyn Committee as: "The prudent man, it is true, would not regard the whole of the annuity as income; but it is likely that in many cases he would be content to get back into the same position as if he had merely been subjected to a direct capital tax equivalent to the burden imposed in such a scheme. Frequently, in fact, he might achieve this object at once by selling his annuity. The improvident man, on the other hand, would probably treat the annuity purely as income; while capital, labelled as such, would have some sanctity in his eyes, it is likely that an annuity would only be taken by him as an excuse to spend." But this is no valid argument that the variant of Dalton would, to a great extent, increase the incentive to work and save. The Colwyn Committee has only looked at the problem from two points of view: of the prudent and the impro-

vident. We are concerned only with the prudent man and his incentive to work and save. So far as he is concerned, he cannot but put in more effort and see that the lapse of the annuity does not reduce his descendants to poverty. He would be prompted to acquire by himself some property during his lifetime, for the benefit of his children and nearest relatives. Would it not under those circumstances increase the ability to work and save?

The Colwyn Committee in its comparison of the Rignano scheme with the proposal of Dalton came to the conclusion: "Under the Rignano scheme an extra burden of duty is imposed at the second transmission, and does not affect the amount of property passing at the first. Under Dr. Dalton's proposal, the corresponding extra duty is taken at the first transmission, and reduces the amount of capital wealth in the hands of the beneficiary. It is true that the beneficiary does not lose in immediate income, but the capital value of his annuity is less than that of the property he has handed over. Thus, the extra burden is imposed on the first transmission, and the distinction made by the Rignano scheme between saved and inherited wealth is blurred. In brief, while Dr. Dalton by taking the extra duty at once, avoids certain flaws in the Rignano scheme, and especially its lack of adaptation to changing values it appears to us that in doing so, he sacrifices much of its essential character". * Dr. Dalton did not differentiate between saved and inherited wealth, as he was, in fact, anxious to see the whole problem from one point of view of the state limiting much of the revenue in case the inherited property before the second transmission is dissipated. Thus, while ignoring the most important point in Rignano's scheme, he has given undue consideration to the revenue yielding capacity of death duties.

Several protests have been raised regarding this scheme, wherein the state has to function as a part of the trustee for a heterogeneous mass of interest. Mr. J. M. Keynes was of opinion that the administration of the trustee's

* Colwyn Committee Report, p. 317.

securities was most efficiently carried out not by a few enormous investment trusts but by a comparatively large number of smaller trusts, each being responsible for several securities. † The Board of Inland Revenue was of opinion that there would not be much difficulty from the administrative point of view if only the proposal were to be limited to benefits taken absolutely under the will or intestacy of a deceased person. It has also expressed its opinion that in case this was extended to gifts *inter vivos* and other interests, there would be insuperable difficulties for administration. Sir O. E. Niemeyer stated that the supplementary levy which might assume the form of cash, government or other approved securities, it would result eventually in "considerable administrative difficulties and would be likely to land the state in a loss because it has got to take a risk on the securities and has to take a risk on the selling of the land." Thus, if this variant scheme of Dalton is to be adhered to, it must be amended considerably for the convenience of the administration.

Mr. A. D. Henderson has a similar proposal. He suggests the imposition of re-inheritance duty in addition to the existing estate duty, payable on the death of the legatees or inheritors and graded according to the amount of the inheritance. A sum equal to the re-inheritance duty is to be handed to the government immediately, either in cash or in the form of securities and the income and principal from it will be paid to the beneficiaries during their life time only.

Mr. Wedgwood suggests that the existing legacy and succession duties be replaced by a progressive tax on all considerable inheritances and gifts and the tax be paid as far as possible when the inheritance or gift tax is received. Such a tax is not likely to discourage work and saving unless the rate of progressive tax becomes very steep. He further suggests that in cases where the rates of inheritance tax are high a certain portion of the tax should be payable at the will of either testator or heir not immediately but after a certain fixed term say, of 20 years. If the tax is

† Silverman: Taxation, Its Incidence & Effects, p. 221.

paid at the end of that period, the sum payable would not of course be the same as in the case of immediate payment but that accrued at compound interest.

United Kingdom

In the United Kingdom, out of the number of different death duties, only three have been in force since 1914: the estate duty which is by far the most important and which is payable on the value of the estate without any regard to its description; the legacy and succession duties which are payable by beneficiaries in connection with the acquisition of property. The legacy duty takes into consideration movable property and money inherited by the legatee, and the succession duty is levied upon immovable property. For practical purposes, both of these are taken to be as one duty.

There are two kinds of estate duty, *ad valorem* and the fixed. The first was levied on the net value of the property. It is graded so that the burden of the duty is distributed on estates proportionately: large estates paying high rates. The British Estate Duty is a highly progressive one, graduated according to the value of the estate. When it was first introduced in 1894, the rates were:

Where the principal value of the estate						Estate duty payable at rate per cent.
Exceeds	£ 100	but does not exceed			£500	£ 1
,,	500	,,	,,	,,	1,000	2
,,	1,000	,,	,,	,,	10,000	3
,,	10,000	,,	,,	,,	25,000	4
,,	25,000	,,	,,	,,	50,000	4 10 sh.
,,	50,000	,,	,,	,,	75,000	5
,,	75,000	,,	,,	,,	100,000	5 10 sh.
,,	100,000	,,	,,	,,	150,000	6
,,	150,000	,,	,,	,,	250,000	6 10 sh.
,,	250,000	,,	,,	,,	500,000	7
,,	500,000	,,	,,	,,	1,000,000	7 10 sh.
,,	1,000,000				—	8

Thus, an exemption of £100 has been fixed. Before 1914, the rates increased from 1 to 15%, the maximum being reached on an estate worth over £1,000,000. In 1914, the maximum rate ran to 20%. In 1919, there was a phenomenal increase and the levy reached 40%

on estates over £2,000,000. In 1930, it shot up to 50%, in April 1939 to 55%; and in July 1940 to 65%. In July 1940, the rates were:

Principal value of the Estate					Rate per cent. of duty
Exceeding	£100	but not exceeding		£ 500	1
"	500	"	"	1,000	2
"	1,000	"	"	5,000	3
"	5,000	"	"	10,000	4
"	10,000	"	"	12,500	6
"	12,500	"	"	15,000	7.2
"	15,000	"	"	18,000	8.4
"	18,000	"	"	21,000	9.6
"	21,000	"	"	25,000	10.8
"	25,000	"	"	30,000	12.0
"	30,000	"	"	35,000	13.2
"	35,000	"	"	40,000	14.4
"	40,000	"	"	45,000	15.6
"	45,000	"	"	50,000	16.8
"	50,000	"	"	55,000	19.5
"	55,000	"	"	65,000	20.8
"	65,000	"	"	75,000	22.1
"	75,000	"	"	85,000	23.4
"	85,000	"	"	100,000	24.7
"	100,000	"	"	120,000	26.0
"	120,000	"	"	150,000	28.6
"	150,000	"	"	200,000	31.2
"	200,000	"	"	250,000	33.8
"	250,000	"	"	300,000	36.4
"	300,000	"	"	400,000	39.0
"	400,000	"	"	500,000	41.6
"	500,000	"	"	600,000	44.2
"	600,000	"	"	800,000	46.8
"	800,000	"	"	1,000,000	49.4
"	1,000,000	"	"	1,250,000	52.0
"	1,250,000	"	"	1,500,000	54.6
"	1,500,000	"	"	2,000,000	58.5
"	2,000,000	"	"	—	65.0

From April 10, 1946 the rate structure has undergone a complete change, and the exemption has been raised from £100 to £2,000. There is no change in the rates paid on estates ranging from £7,500 to £12,500 and the duty is regraded from £2,000 to £7,500. Estates above £12,500 have their rates regraded upwards till a limit is reached where an estate of over £2,000,000 will be liable to a 75% duty instead of the previous 65%. Thus, on medium sized estates, the duty imposed was somewhat lighter and on larger estates even more steeply progressive. One

per cent. is paid at £2,000; 12% at £20,000; 24% at £50,000; 35% at £100,000; 50% at £250,000; 70% at £1,000,000; and 75% at £2,000,000. Earlier we have observed the effects of these changes. Now we will do well to emphasise the part that death duties play in the tax structure of the United Kingdom. The yield of death duties was as follows:

Years :	1938	1914	1945	1946	1947	1948
Yield : (£ million)	78	107	119	142	163	160

Legacy and succession duties are paid on inheritance after deduction of estate duty according to the relationship of the beneficiary. The rate at which the duties are chargeable is determined by the relationship of the beneficiary to the author of the benefit. The rates at the time of the Colwyn Committee were:

1% where the beneficiary is the husband, wife or lineal issue or ancestor of the author of the benefit, subject to exemption where the total value of the property passing does not exceed £15,000, or where the total individual benefit does not exceed £1,000, or, in some instances, £2,000.

5% where the beneficiary is a brother or sister, or a descendant of a brother or sister.

10% in all other cases.

But at present in Britain, husband, wife, lineal-descendants or ancestors pay 2%; brother, sister, or other descendants 10%; and charities 10%; and any other beneficiaries 20%. These were the rates introduced in 1947.

United States of America

The Federal Estate Tax of 1915 was introduced in U.S.A. not upon the property but on the transfer from the decedent to beneficiaries. That tax applied to the entire estate and not in particular to legacies or the distributive shares. One of the main hall-marks of this estate tax is that there was no differentiation on the basis of the value of separate interest or the relationship of the beneficiary to the decedent. The rates were as follows:—

Rate per cent.	Net total.
1	Under $50,000
2	$50,000 to $150,000
3	$150,000 to $250,000
4	$250,000 to $450,000
5	$450,000 to $1,000,000
6	$1,000,000 to $2,000,000
7	$2,000,000 to $3,000,000
8	$3,000,000 to $4,000,000
9	$4,000,000 to $5,000,000
10	$5,000,000 and over.

The model inheritance tax proposed in 1922 by the committee on inheritance tax of the National Taxation Association was:

Schedule of State Inheritance Tax Rates suggested. *

Brackets of taxable amounts in excess of exemption †	Classes of beneficiaries A.	B.	C.
Over $25,000	1x	2x	6x
Over $25,000 but not over $50,000	2x	3x	7x
Over $50,000 but not over $100,000	3x	4x	8x
Over $100,000 „ „ „ $500,000	4x	5x	9x
Over $500,000	5x	6x	10x

Class *A* to include surviving spouse, lineal ancestors or descendants, adopted child or lineal descendant of adopted child, step-child, daughter-in-law, son-in-law.

Class *B*, brother, sister, brother-in-law, sister-in-law, nephew, niece, lineal descendants of niece (probably also of nephew), wife or widow of a nephew, husband of a niece, institutions within the State.

Class *C*, any other person or corporation.

On sums less than $10,000 the Committee suggested a lower rate of 5x for Class *C* beneficiaries.

The above table generalizes most of the Estate Inheritance Taxes in effect today.

The relationship discrimination will be more clear from the rates of the California Inheritance Tax of 1942:

* Letter 'x' serves as a sort of co-efficient to indicate that the actual level would vary from State to State.
† Exemptions: Class A, $100,000; Class B & C, $500.

CALIFORNIA INHERITANCE TAX, 1942

Relationship of beneficiary to deceased.	Exemption.	Rates applicable to the fraction of the inheritance in excess of exemption from						
		0 to	25000 to	50000 to	100000 to	200000 to	300000 to	500000 to
	$	25000	50000	100000	200000	300000	500000	and up.
Class A								
Wife*	25.000	2%	3%	4%	7%	9%	9%	10%
Minor child	12,000	2%	3%	4%	7%	9%	9%	10%
Husband, other child, parents, grand parents, grand children.	5,000	2%	3%	4%	7%	9%	9%	10%
Class B								
Brother, sister or descendant of either; son-in-law, daughter-in-law.	2,000	5%	7%	10%	12%	12%	14%	15%
Class C								
Uncle, aunt, or descendants of either.	500	6%	9%	12%	12%	12%	15%	15%
Class D								
All others†	50	7%	10%	12%	12%	12%	15%	16%

* One half of the community property is also exempt.

† Does not include charitable bequests; these are entirely exempt.

(The foregoing table is adapted from the Report to the Joint Committee on Internal Revenue Taxation, Federal and State Death Taxes, Washington, 1933, p. 87, and Tax System p. 301).

In the United States of America, the estate is based on the net value of an individual's property which is transferred to others at the time of death. The Schedule I to the Estate Tax (1926 Act as amended—specific exemption of $100,000 in determining the net estate) is:

	Per cent.
First $ 50,000 of net estate	1
In excess of —	
$ 50,000 up to $ 100,000	2
100,000 up to 200,000	3
200,000 up to 400,000	4
400,000 up to 600,000	5
600,000 up to 800,000	6
800,000 up to 1,000,000	7
1,000,000 up to 1,500,000	8
1,500,000 up to 2,000,000	9
2,000,000 up to 2,500,000	10
2,500,000 up to 3,000,000	11
3,000,000 up to 3,500,000	12
3,500,000 up to 4,000,000	13
4,000,000 up to 5,000,000	14
5,000,000 up to 6,000,000	15
6,000,000 up to 7,000,000	16
7,000,000 up to 8,000,000	17
8,000,000 up to 9,000,000	18
9,000,000 up to 10,000,000	19
10,000,000 ———	20

The additional estate tax (1932 Act as amended—specified exemption of $60,000 in determining the net estate is) is:

First $5,000 Net Estate		Per cent. 3 Tax on lower amount	Per cent. on excess
$ 5,000 to	10,000	$ 150	7
10,000 to	20,000	500	11
20,000 to	30,000	1,600	14
30,000 to	40,000	3,000	18
40,000 to	50,000	4,800	22
50,000 to	60,000	7,000	25
60,000 to	100,000	9,500	28
100,000 to	250,000	20,700	30
250,000 to	500,000	65,700	32
500,000 to	750,000	145,700	35
750,000 to	1,000,000	233,200	37
1,000,000 to	1,250,000	325,700	39
1,250,000 to	1,500,000	423,200	42
1,500,000 to	2,000,000	528,200	45
2,000,000 to	2,500,000	753,200	49
2,500,000 to	3,000,000	998,200	53
3,000,000 to	3,500,000	1,263,200	56
3,500,000 to	4,000,000	1,543,200	59
4,000,000 to	5,000,000	1,838,200	63
5,000,000 to	6,000,000	2,468,200	67
6,000,000 to	7,000,000	3,138,200	70
7,000,000 to	8,000,000	3,838,200	73
8,000,000 to	10,000,000	4,568,000	76
10,000,000 and over		6,088,200	77

Gift Tax: In U.S.A., individuals who make gifts are subject to a gift tax. It is based upon the value of the property given. During his lifetime, an individual may give away $30,000 tax free. Over and above this exemption, the first $3,000 of gifts to each beneficiary in any one year is also exempt. The value of gifts is taxed at the following rates:—

A Amount of net gifts equalling.	B Amount of net gifts not exceeding.	C Tax on amount in column (A)	D Rate of tax on excess over amount in Col. (A) per cent.
$	$	$	
. . . .	5,000		2 1/4
5,000	10,000	112.50	5 1/4
10,000	20,000	375.00	8 1/4
20,000	30,000	1,200.00	10 1/2
30,000	40,000	2,250.00	13 1/2
40,000	50,000	3,600.00	16 1/2
50,000	60,000	5,250.00	18 3/4
60,000	100,000	7,125.00	21
100,000	250,000	15,525.00	22 1/2
250,000	500,000	49,275.00	24
500,000	750,000	109,275.00	26 1/3

750,000	1,000,000	174,900.00	27 3/4
1,000,000	1,250,000	244,275.00	29 1/4
1,250,000	1,500,000	317,400.00	31 1/2
1,500,000	2,000,000	396,150.00	33 3/4
2,000,000	2,500,000	564,900.00	36 3/4
2,500,000	3,000,000	748,650.00	39 3/4
3,000,000	3,500,000	974,400.00	42
3,500,000	4,000,000	1,157,400.00	44 1/4
4,000,000	5,000,000	1,378,650.00	47 1/4
5,000,000	6,000,000	1,851,150.00	50 1/4
6,000,000	7,000,000	2,353,650.00	52 1/2
7,000,000	8,000,000	3,878,650.00	54 3/4
8,000,000	10,000,000	3,426,150.00	57
10,000,000		4,566,150.00	57 3/4

Thus, the yield of the estate and gift taxes is great, particularly in view of the State as well as the Federal revenues:

Revenue by States, by Source, 1945

(in million $)

	Death & Gift taxes	Total Revenue
United States	135.7	4,778.4
New England	16.0	288.2
Mid. Atlantic	54.8	1,129.4
E. N. Central	26.0	940.8
W. N. Central	6.6	400.0
South Atlantic	8.6	544.6
E. S. Central	3.0	244.3
W. S. Central	4.6	431.1
Mountain	2.6	169.0
Pacific	13.4	630.9

Federal Revenue by Source, 1938-48

(in million $)

Year	Estate & Gift Taxes
1938	417
1939	361
1940	360
1941	407
1942	433
1943	447
1944	511
1945	643
1946	677
1947	779
1948	788

AUSTRALIA

In Australia, the Commonwealth Estate Duty Act, (1914), and the Estate Duty Assessment Act, (1914-28), impose a duty on the estates of deceased persons, the net value of which exceeds £1,000. According to the Estate Duty Assessment Act, (1940), the Estate Duty Assessment Act, (1914-28) was amended, so as to allow the following exemptions:

(a) Where the value of the estate passes to the widow, children, or grand children of the deceased, the sum of £2,000 decreasing by 1 for every 10 by which the value exceeds £2,000 up to £10,000, and thereafter decreasing by 1 for every 2 by which the value exceeds £10,000;

(b) Where no part of the estate passes to the widow, children or grand children, the sum of £1,000 decreasing by 1 for every 10 by which the value exceeds £1,000 up to £6,000, and thereafter decreasing by 1 for every 8 by which the value exceeds £6,000; and

(c) Where part only of the estate passes to the widow, children, or grand children, the statutory exemption is to be calculated proportionately under (a) and (b).

Under the Estate Duty Act, (1940), the following rates have been prescribed:

Value in £	Rate imposed
1 to 10,000	3%
10,001 to 20,000	3% to 6%
20,001 to 100,000	6% to 18%
100,001 to 500,000	18% to 20%
Over 500,000	20%

By the Estate Duty Act, (1941) these rates were amended as under:

Value in £	Rate imposed
1 to 10,000	3%
10,001 to 20,000	3 to 6%
20,001 to 120,000	6 to 26%
120,001 to 500,000	26 to 27.9%
Over 500,000	27.9%

At that rate, the following has been the revenue from the source of estate duty of the Commonwealth of Australia:

Year	Revenue (In thousand £)
1938-39	1,915
1942-43	2,696
1943-44	2,761
1944-45	3,090
1945-46	3,880
1946-47	4,019

National Estate Duty: Assessment Year 1945-46

Grade of dutiable value in £	No. of estates.	Gross value as assessed in £	Dutiable value in £	Net duty Payable in £
1 to 1,000	3,097	8,953,339	1,240,061	37,299
1,001 to 2,000	1,617	5,607,864	2,353,728	70,374
2,001 to 3,000	964	4,402,367	2,362,885	71,036
3,001 to 4,000	691	3,917,514	2,389,599	71,363
4,001 to 5,000	494	3,331,682	2,211,764	66,150
5,001 to 10,000	1,194	11,292,858	8,338,163	250,067
10,001 to 20,000	788	13,383,974	11,129,413	488,834
20,001 to 50,000	376	13,749,311	11,088,683	919,203
50,001 and over	96	11,515,306	8,982,063	1,837,518

CANADA

In the Dominion of Canada, inheritance taxes constitute a provincial head of revenue, despite the fact that the Royal Commission on Dominion-Provincial relations recommended that it should be a solely federal tax. The constitutional limitation that the provinces should restrict themselves to direct taxation within their respective jurisdiction raised many complicated issues. Succession duties were first imposed in Canada under the Succession Duty Act, Cap: 14, Statutes of 1940-41, and provision was made for two forms of duties: one initial and the other additional. For determining the additional duty, beneficiaries were divided into the following four classes:

Class A: The widow, or the child of the deceased.

Class B: The grandfather, grandmother, father, mother, husband, son-in-law, or daughter-in-law, or a child of the deceased who does not come under Class A.

Class C: Lineal ancestors, brothers or sisters of deceased, or a descendant of them, or aunts and uncles and any descendant of them.

Class D: Any person of any degree of consanguinity to the deceased, not included in the other classes, and strangers in blood.

In Canada, no duty is payable on estates not over $5,000, or on bequests not exceeding $1,000 to any one individual. Widows are exempt up to $20,000 plus $5,000 for each dependent child, unless the child also benefits, in which case the exemption for such a child is $5,000 less the amount of the benefit. A child is exempt to the extent of $5,000, but in the case of a child having no surviving parent it is $15,000 in addition to the $5,000. In cases, where there is more than one such dependent orphan, the $15,000 exemption is apportioned among them.

The rate is determined by (i) the size of the estate, (ii) the size of the amount which the individual receives, and (iii) by the consanguinity of the heir. The initial rates dependent on the aggregate net value began at ½% applicable on estates in excess of $25,000, and increased by totality until the maximum rate of 10% was reached on estates exceeding $5,000,000 of aggregate net value. The additional rates dependent upon dutiable value and determined by the size of the individual bequest and the relationship of the beneficiary to the deceased, starts at 2% on succession of a dutiable value exceeding $5,000 to Class *A* beneficiaries, and 1%, 2% and 2½% on successions in excess of $1,000 to Class *B*, *C* and *D* beneficiaries respectively. The additional rates increase by totality until a maximum rate of 17% is reached upon a dutiable value in excess of $5,000,000, $3,000,000, $2,000,000and $1,500,000 for beneficiaries in Classes *A*, *B*, *C* and *D* respectively.

Quebec: Under the current legislation in *Cap*: 80, revised statutes of 1941 (as amended), the rate of duty depends upon, firstly, the net value of the estate; secondly, the relationship of the deceased to the beneficiary; and

thirdly, the amount passing to each individual beneficiary. In Quebec, the beneficiaries have been divided into three classes:

Class 1: Lineal ancestors and descendants, husband, wife, father-in-law, mother-in law, son-in-law, daughter-in-law, step-father, step-son or step-daughter.

Class 2: Brothers, sisters, descendants of brother or sister, parent or child of such brother or sister.

Class 3: Other persons.

The rates in Quebec are:

"Estate-based" Rates

Rate	Class 1	Class 2	Class 3
Minimum Rate %	1	4	10
Aggregate Value $	10,001	1,001	———
Maximum Rate %	15	20	30
Aggregate Value $	1,000,000	1,000,000	1,000,000

"Share-based" Rates

Rate	Class 1	Class 2	Class 3
Minimum Rate %	1	1	2
Value of Share $	10,001	1,001	———
Maximum Rate %	10	10	5
Value of Share $	1,400,000	1,500,000	1,200,000

In the above rate structure, the progression is gradual, increasing by fractional percentages.

Ontario: Under the current legislation in Ontario of *Cap*: 1, statutes of 1939 (as amended), the rates of duty depend upon, firstly, the aggregate value of the estate; secondly, the relationship of the deceased to the beneficiary; and, thirdly, the amount passing to each individual beneficiary. The beneficiaries in this province have been divided into three classes:

Class 1: Grandfather, grandmother, father, mother, husband, wife, child, son-in-law and daughter-in-law.

Class 2: Lineal ancestors, except those in Class 1, brother, sister, descendant of brother or sister, brother or sister of deceased's parents and descendants of such brother or sister.

Class 3: Other persons.

"Estate-based" Rates.

Rate	Class 1	Class 2	Class 3
Minimum Rate %	1	5	7 ½
Aggregate Value $	75,001	10,001	5,001
Maximum Rate %	14	17	35
Aggregate Value $	5,000,000	1,000,000	800,000

"Share-based" Rates.

Rate	Class 1	Class 2	Class 3
Minimum Rate %	1 1/2	2 1/2	
Value of Share $	50,001	10,001	
Maximum Rate %	15	13	
Value of Share $	3,000,000	3,000,000	

In addition, a surtax of 15%, 20% and 25% of the amount of duty payable is imposed by the Act upon Classes 1, 2 and 3 respectively. Here, also progression is gradual, increasing by fractional percentages.

This form of taxation has become important in the provincial revenue structure. They contribute a higher proportion of aggregate provincial revenue in Quebec and Ontario than those in other provinces, the percentages for 1939 being approximately 21 in Quebec and 13 in Ontario.

The following figures show clearly how succession duty revenue of the Dominion and Provinces has increased:

Succession Duty Revenue
Dominion & Provincial
(In thousand $)

Year:	1913	1929	1933	1937	1939	1941	1943
Quebec	1,605	5,294	2,755	11,992	12,056	12,202	6,624
Ontario	1,146	6,610	8,081	20,214	11,500	11,677	13,320
Manitoba	268	1,034	424	402	875	735	341
Sum-total of all Provinces:	3,611	15,849	12,745	36,689	27,850	27,377	24,391
Dominion of Canada:	...	...	...	...	...	6,957	15,020
						34,334	39,411

This universal fiscal instrument of death duties has come to occupy a unique place in the financial armoury of any country. It has many similarities in all parts of the world. In U.K., the estate and succession duties are levied by the Central Government only. In U.S.A., death duties are imposed both by the Federal and the State authorities. In Australia, these taxes are levied by the Federal Government and also by each State in general. Australian legislation imposes taxes of the type of estate duties rather than of the succession duties. In Canada, these taxes form part of the provincial field.

In the United Kingdom, the rates are severe for estate duties and a large proportion of revenue comes from death duties. In U.S.A. the Federal Government's levy on the estates is characterised as highly progressive, with relatively high exemption limits. According to the Australian Duty Assessment Act, the exemptions belong to the category of deduction rather than that of the starting point which is prevalent under the Canadian legislation. Provision is also made in Australia for a decrease in the exemption; as the size of the estate increases, the exemption being completely absorbed. *

* Reference Book for Dominion-Provincial Conference on Reconstruction, "Succession Duties".

CHAPTER 6.

JURISDICTION AND ADMINISTRATION

1. Jurisdiction of Death Duties. 2. Arguments in Favour of State Jurisdiction. 3. Arguments in Favour of Federal Jurisdiction. 4. Administration of Death Duties. 5. Double Taxation. 6. Evasion & Avoidance. 7. Administration in some Important Countries.

Jurisdiction of Death Duties

Sufficient attention is not yet bestowed on the problem of jurisdiction of death duties. There are constitutional difficulties because of the entry of either of the Federal or the State Governments into the field earlier than the other, and when once the Federal or the State Government has entered into death taxation, it is taken for granted that the sole right is vested in that taxing authority.

Arguments in Favour of State Jurisdiction

"By tradition, legal theory and revenue necessity", death duties belong to the State authority. This was the argument advanced by some representatives who appeared before the Ways & Means Committee of the House of Representatives in U.S.A. As the States have entered into the field earlier than the Federal Government, death duties belonged to the jurisdiction of the former. This however is not a sound argument. The justification of levying a particular tax does not depend entirely on tradition. When once a tax is already imposed, it is easy to justify it on grounds of tradition.

It is said that the State has the ultimate title to land and other property. In fact, death duties have been generally regarded "not as direct taxes on property or income but as excises on the transfer of property." This is the judicial opinion as far as the Federal taxes are concerned. The Committee on Post-war Tax Policy in its "A Tax Programme for the Solvent America" (1945),

observed that the excise on the transfer should be levied by that jurisdiction which grants the privilege of transfer. In U.S.A. that authority which grants the privilege for transmissions of property vests with the States. Under the State law, property at the time of death of the decedent is transmitted to his heir, and in case there is no heir to the decedent, the property escheats to the public authority which happens to be the State. From the administrative angle, it can be stated that the States will have easy access to all information regarding the estates than the Federal Government. "Modern enterprise often brings different parts of an organic commercial transaction within the taxing power of more than one state, as well as that of the nation. It does so because the transaction in its entirety may receive the benefit of more than one government. And the exercise by the States of their Constitutional power to tax may produce difficult political and fiscal situations. But they are inherent in the nature of our federalism and are part of its price. These problems are not peculiar to us. Kindred problems have troubled other constitutional federalism."

For purpose of revenue, it is the States or Provinces that have less financial resources and relatively more need for revenue than the Federal Government. The Federal Governments also have been, while strengthening their own fiscal positions, collecting taxes which should ordinarily fall into the States or Provincial categories. In India, it is assumed that the provinces, for the aid of which the Centre wishes to enact the Estate Duty Bill, will be the recipient of this revenue. One of the main objects in imposing the levy is that it would help the post-war reconstruction plans of provinces. As the Federal Government has several other sources, the provinces must be given exclusive rights to levy taxes like death duties.

Arguments in Favour of Federal Jurisdiction

On the other hand, there are several arguments in defence of Federal jurisdiction of death duties. When the Federal Government imposes the death duties, an uniform

system of the same can be evolved throughout the country. When the states have their own individual rates of duties, considerable diversity of legislation among the states would be witnessed, as in Canada and Australia where the rates of duties, the exemption limits and the classification of beneficiaries, differ from province to province and State to State, with the result that severe complications arise in collection and imposition. A millionaire before his death would prefer to get his property transferred to a State wherein the rate of duty and the exemption limit would be favourable for his descendants. There would be transfer of property from one Province or one State to another, with the result of inequality of the incomes accruing from the source. In the case of millionaire who accumulated his property in one State and who before his death had it transferred to another State, the former state should naturally have the benefit to levy the tax, whereas actually the second State becomes richer by it. In addition, there might be overlapping jurisdiction and consequently multiple taxation might arise. The imposition of the tax by the State or Provinces thus brings about confusion and inequalities of multiple taxation. But in some countries, like the U.S.A., this argument is losing much of its previous weight, for by means of mutual forbearance and reciprocal and other suitable legislation, the States have gone a long way towards solving the problem of double taxation of the intangible property of non-resident descendants. There is, however, reason to believe that, given the opportunity, the States will succeed in solving this problem or reducing it to a minimum. Another argument in defence of Federal death duties is, as Groves points out, that it makes for a more equitable distribution of death tax revenue and the benefits resulting therefrom. He says that some States like New York would procure relatively a larger revenue from the tax while others like North Dakota and other States would derive but meagre revenue from it. "For example, when a wealthy manufacturer of tobacco died not long ago, it was felt that since his large estate had been built by

contributions from tobacco farmers and consumers in many parts of the country, it should not be earmarked for any one State just because he happened to have resided there. Similarly, a person might make a fortune harvesting the natural resources of a particular State and move to another shortly before his death." With the imposition of death duties by the Federal Government as a source of its own revenue or for ultimate distribution of the proceeds of the same, a greater benefit naturally results therefrom.

The third facet of the problem of jurisdiction is whether it would not be possible for the States as well as the Federal Government to levy death duties. This argument has been advocated on the ground that those persons who move freely from State to State with a view to escape the tax can be dealt with by the Federal Government which does not suffer from any limitation of jurisdiction. It may not be more effective if the Federal Government along with the provinces or the States choose to enter the field of death duties without any intention of competing with the other Governments. Moreover, in cases, where the States push their tax rates to exhorbitant heights, the Federal Government can come to the rescue of the tax payers by bringing down the rates, on the one hand, or, on the other revise them if the Federal Government considers that the tax rates should be increased to aid in the socialization of property or equal distribution of property or wealth. It can impose a heavy tax on transmission of estates and can also compel the States to increase their tax rates on legacies and successions. The rates of death duties can be stable under those circumstances with the minimum of changes from year to year.

There are several strong economic arguments in favour of federal taxation. The accumulation of large estates are the result of national activity, and the administration of death duties by the federal government would be more desirable than that of the States. Moreover, in the large estates, the States would always be beset with jurisdictional difficulties, each state being afraid to

go further than its neighbours with the result that the scale of rates may not realize the legitimate possibilities of death taxation. It is a common argument that the State death duties are less progressive. To add to this, the jurisdictional limitations in the case of States, in taxing such types of property as intangibles, bank deposits, movable personal property, etc., which might fall within the jurisdiction of another State, bring in their wake several difficulties. Inter statal arrangements might aid them in overcoming those obstacles. "The objections to multiple administration establishing forty-nine sets of officers for one tax—are important not in themselves but principally because each set operates a tax which is somewhat different from every other. If, by some miracle, uniformity in State death taxes could be achieved, multiple administration would not in itself be disadvantageous. The reason is that complete centralization in the hands of the federal government would pose a difficult task. In the past, federal administration of the death tax has been criticised as bureaucratic and slow moving. Large scale administration requires multiplication of rules, which in an individual case, may hamper a prompt and equitable settlement. In some States the quality of the officials is excellent, and, since the task is of moderate dimensions, administration is superior to that at Washington. This fortunate occurrence should not, however, disguise the fact that no major State tax is 'more poorly administered than the death tax, whether judged by principles of organization, by equity of application, or by available quantitative measures'". *

But the best way seems to be that the estate tax while being under the federal jurisdiction should, as in the case of the incomes, be distributed among the provinces in an equitable proportion. This would not only remove the disadvantages or the defects in State taxation but would obtain the advantages of federal death taxation. While evasion and avoidance can be stopped,

* James A. Maxwell: The Fiscal Impact of Federalism in the United States.

the productivity of the same can be increased. Similarly, multiplicity and diversity of taxation can be removed and greater uniformity can be maintained. The best way in dealing with the jurisdiction of death duties is therefore by imposing the tax as a federal one and distributing equitably the proceeds amongst the provinces or the States. They then among themselves can come to some understanding for allocation of the proceeds of the death duties, giving the power to the federal government for collection. The American Committee in its Report stressed the same argument: "On strictly logical grounds a very strong case could be made for separation of sources as a co-ordination device in the death tax field. If this were recommended, the federal government would be the choice as the taxing unit. The State tax is plagued by inter-state competition and multiple taxation, and especially by the fact that estates are highly concentrated in a relatively few States, though the wealth represented may have been accumulated over a much wider area. On the other hand, the States, with one exception, have a proprietary interest in this field and any proposal for surrender would rouse intense antagonism. Moreover, any method of getting the States out of the field, short of a constitutional amendment, would involve a distribution of revenues not very different from the present". *

Federal Estate Tax Credit: In some federations, death duties are co-ordinated by a system of credit. By this is meant, that the deceased's estate duty is given a credit as against the duty imposed by the Federal Government, to the full extent of the death duties paid to the States. The credit that was allowed by the federal government could be up to 80%. There is also an agreement in regard to the matters of exemptions that have to be given to the Provinces or the States, and it would endeavour to strengthen the administration, thereby avoiding any possibility for double or multiple taxation.

* Senate Document No. 69, 78th Congress—Report of Committee on Intergovernmental Fiscal Relations, Major Conclusions and Recommendations, Vol. i, Chap. iv.

The strong arguments in defense of the method of credit are firstly, "the credit softens the burden of the federal state tax and permits the states to levy correspondingly heavier death taxes" and secondly, "the credit clause is more potent". Though several times there were dissensions and though on several occasions some states began reducing the rates of the estate taxes, it must be said that competition between the states and the federal government has been lessened with the aid of this credit clause. It was also stated that the effect of the clause was to make the duty highly productive.

Administration of Death Duties

The problem of the administration of death duties is a very vexatious one, as the diversity and the multiplicity of bases for its taxation bring about numerous administrative considerations, particularly when the states and the federal governments engage themselves in similar taxation. It would be very difficult to arrive at a common basic standard out of:—

a) nationality of the decedent;
b) domicile of the decedent;
c & d) nationality or domicile of the heir;
e) situs of the property involved; and
f) the corporate location of property or business enterprise.

The basic standard of nationality is the oldest, but it affords an unreliable standard in death taxation. Till 1914, this principle was taken kindly by countries like Germany, Norway, Sweden etc., but, later on, with the advent of reliable basic standards and because of the administrative difficulties, nationality could not be taken as the only criterion in the levy of death duties. The difficulty about it is that it would be easy for non-resident decedents to escape taxation. It is not justifiable that a person, whether a foreigner or a domicile in one state, who has property within its frontiers, should evade or avoid paying the death taxes, on the ground of nationality. At present, the basis of nationality conforms to the German National

Inheritance Taxation, where if the decedent happens to be a foreigner resident in Germany, he will not be taxed on the real property and other assets which are located outside the frontiers of Germany.

More reliable than nationality is the principle of residence or domicile. It necessarily means the permanent residence rather than a temporary one which is not a dependable test in the imposition of death duties. The Economic and Financial Committee of the League of Nations had recommended death duties to correspond to the basis of domicile. On the requisite period of residence or domicile of the decedent, nothing has been agreed internationally. American courts have given bare rulings on evidences of the decedent's intent, and have been in opposition to the fixation of any arbitrary period. The basic standard is convenient from the administrative point.

Three arguments have been adduced by Shultz in defence of the basis of domicile or residence: Firstly, if the government were to depend solely on the permanent residence, there might be an insufficient revenue even for the mere protection of property. Secondly, most of the revenues of the resident population might be derived from outside sources, e.g. from the business conducted in other states or countries in which case the home government would be gaining at the expense of its neighbours. Thirdly, property owners, like absentee-landlords or the stock holders of railways cannot be declared devoid of all complications to the place whence their profits are derived. In matters like jewellery, cash, clothing, etc., this principle of domicile has no objection. The American Federal Treasury regulations are also quite clear and Article 4 reads: "The statute takes no account of the citizenship of the decedent, but prescribes different rules according to whether the decedent was a 'resident' or a 'non-resident' of the United States. . . A person is 'resident' of the United States for the purpose of this tax, only in case he had a domicile therein at the time of his death. A person acquires a domicile in a place by living there for even a period of time, with no definite present intention

of removing therefrom. Residence without the requisite intention to remain will not suffice to constitute domicile, nor will intention to change domicile effect such a change unless accompanied by actual removal". The principle of domicile was early established by the Supreme Court of the United States as a very satisfactory and legitimate one for inheritance taxes. It has been emphasised that till today most of the States based their death taxation on this basis.

Since the beneficiary is also, to a great extent, involved in the imposition of death duties, his nationality or domicile must be considered. The taxing authority should fix death duties on the basis of the nationality of the descendant or the inheritor, who pays the tax. This is once again a very unreliable standard to conform, particularly because it does not consider the decedent who was responsible in the accumulation of the inherited property. The tax should be imposed on the property, which is the result of the exertions of the decedent and not on any considerations of the domicile or the residence of the inheritor. It is doubtful whether the beneficiary should be taxed according to his domicile or residence, irrespective of any consideration of the decedent. It is the experience of the governments of some important countries that it is difficult and costly to obtain information relating to the transmission of property through inheritors. Avoidance and evasion would be common under such circumstances, particularly when it would be difficult to know the inheritor, his nationality and domicile or his residence.

To come to the situs of the property involved; in the United States, the Committee appointed by the National Tax Association emphasised that "the correct principle underlying the taxation of inheritances is expressed by saying that a given State should levy its inheritance tax only with reference to such property as devolves in accordance with its laws"; it can be based on the situs for real property and domicile for most of the personal property. In other words, the real property would be taxed by that government where it was located. The first

economist who stood in defence of this standard was George Schanz who, though at first was of the opinion that the situs of the property to be the most reliable standard , was ultimately reconciled to the principle of domicile of the decedent on grounds of administrative difficulties. The Italian economist, Tivaroni, recommended situs taxation as against domicile taxation. As the United States of America could not come to a decided agreement regarding a uniform system of taxation, the Supreme Court declared in 1939, in *Curry* vs. *McCanless* that intangible property could be taxed under certain conditions by the State where it is located as well as by the State of the decedent's domicile.

The decision can be explained as follows: "A resident of Tennessee who had reserved the power to change the beneficiaries of a trust in her will, had left stock in trust with a bank in Birmingham, (Alabama) which both States attempted to tax. The court found both taxes vaild as well as affirmed. There are many circumstances in which more than one state may have jurisdiction to impose a tax and measure it by some or all of the taxpayers' intangibles. In *Graves vs· Elliott,* the Court held that both New York and Colorado could tax the securities left in trust by a resident of New York in Colorado when the right was reserved to amend and revoke the trust. Thus, securities with a 'trust situs' may be taxed in two States". Although the Supreme Court made its intentions quite clear, complex problems usually arise in the determination of the domicile of the decedents. It is likely that two States might view differently regarding the domicile of a decedent. Buehler narrates an interesting dispute that arose among the States of Florida, Massachusetts, New York and Texas over the domicile for death taxation of Col. Edward Green. "Green was born in England and died in New York. When he was still young, he went to Texas to look after his mother's interests in a rail road. There he stayed nineteen years, returning then to New York and only occasionally going back to Texas.

But he rented a room in Texas to retain his right to vote there and apparently to avoid taxes, repeatedly declared in legal documents that his residence was in Texas. Yet in Texas he paid no taxes on his personal property or income. Upon leaving Texas, he established a residence in New York and maintained a business office there, but spent little time in his later years in his New York apartment and devoted more of his time to Massachusetts than to any other State. There he lived on his estate and entered into social life with his friends, without paying any income or personal property taxes. Somewhat less time was spent at his Florida Estate, but he never voted in Florida or paid an intangible property tax there, because he claimed he was a resident of Texas. The Supreme Court found that Green's domicile was in Massachusetts and that State alone could collect death taxes from his intangible property. He became a non-resident of Texas when he moved away, lived only temporarily in New York, and never abandoned his Massachusetts domicile for his later Florida domicile. His family, friends and home were thus in Massachusetts in fact as well as in intent. Again the Court, after some possible wavering in previous cases, ruled that a person could have only one domicile at death for purposes of intangibles taxation". *

In taking situs as the basis of death duties, it will be quite clear that there is the definiteness regarding the location of the property and double taxation can be avoided, as there can be only one domicile and one situs. Multiple taxation therefore has no place in death duties, when they correspond to the basic standard of situs. As early as 1889, in England, the Royal Colonial Institute favoured this basis for death duties, reciprocal arrangements between the mother country and the dominions being practically based on situs. Most of the countries found it more convenient to fix death duties on the principle

* Buehler: Public Finance, p. 469-70

of situs and for taxing the securities of domestic corporations held by non-resident decedents. †

Double Taxation

Double taxation is defined as taxation of the same person or property by different taxing authorities or several times even by the same taxing authority. The problem arises with grave consequences when the states impose death duties. In cases where the states as well as the federal government also levy, the problem of multiple taxation makes its appearance. Naturally, it leads to discriminatory taxation, as some tax-payers will be more heavily taxed than others. This is not a little due to the fact that often domicile as well as the situs of the decedent do not coincide, and so double taxation becomes apparent.

In countries where death duties are levied, provision is made for leaving out the possibility of double or multiple taxation. In certain British Possessions, allowance is paid if there is double taxation. It will not exceed the amount of the estate duty payable in Britain on the same property, particularly when the decedent dies domiciled in that country. To take an illustration, let us suppose that *A*, domiciled in New Zealand, has a British settlement with British trustees, beneficiaries, etc. On his death, all the property being in New Zealand, duty is paid there on it. As the form of the settlement is British, estate duty in Great Britain will also be payable, and it is presumed that the New Zealand duty can be allowed against this duty.

In the case of United States of America, the National Tax Association had carried out a continuous campaign for a reciprocity provision by which State *A* would agree to exempt the intangibles of non-resident decedents (i.e. decedents domiciled in State *B*), provided that State *B* would reciprocate. * This campaign met with favour-

† Shultz: Taxation of Inheritance, p. 242

* James A. Maxwell: The Fiscal Impact of Federalism in the United States.

able response and by 1932 nearly 39 States entered into reciprocity arrangements.

In Australia, a provision was made that in cases where duty is lawfully paid in any place outside Australia there shall be deducted from the total duty the lesser of either the amount of duty so paid in the place outside Australia, or the duty that is payable in respect of the estate. In Canada, the taxation of estates by a Canadian province and by the Dominion is a form of double taxation. The death tax legislation has resulted in double or multiple taxation as the bases of the different taxing authorities, (i) the domicile of the decedent and (ii) the situs of the property, do not correspond. As a natural result, an estate, or portions of it is taxed by the two jurisdictions, one imposing duty upon the transmission or transfer of succession and the other upon the property itself.

Evasion and Avoidance

"The administration of death taxes has been a race between taxable decedents, heirs, and their attorneys and administrators, on the one hand, seeking to escape the tax, and tax administrators and legislators on the other, seeking to stop the leaks". * It has been a commonplace phenomenon in the administration of any tax that its evasion and avoidance are patent irrespective of the strict administration and vigilance of the taxing authority. Fiscal evasion has been defined by Justice Holmes thus: "when the law draws a line a case is on one side of it, or the other, and if on the safe side, is none the worse legally that a party has availed itself to the full of what the law permits. When an act is condemned as an evasion, what is meant is that it is on the wrong side of the line indicated by the policy if not by the mere letter of the law." † Thus 'evasion' should be viewed from the angle that Justice Holmes has given, while 'avoidance' should be viewed to embody legally, if not morally, the methods of escaping or avoiding the intent of the Death Duties. Death

* Jensen: Government Finance, p. 413-414.

† Bullen vs. Wisconsin, 240 U.S. 625.

duties might be avoided legally, partly or wholly in several ways.

1) *Hiding*: When transmission of property takes place, it might not be reported to the taxing authority and therefore escapes the tax administrator's attention. This is possible in cases of cash, jewellery and unregistered bonds which enable the easiest form of legal evasion. An alert administration, may not allow this to happen, but the difficulty arises with the question of access to the accounts of the deceased. In almost all the countries the law prescribes that the administrator of death tax should have the power to scrutinize, inspect and go through all forms of property left behind. The decedent on the point of his death will not be much perturbed to instruct the established inheritors to escape and avoid the tax. The inheritor might fly away with the property to another state or country where the inheritance tax was less heavy. There might be flight of capital, but in most of the countries nearly the same rates of death duties are levied. Moreover, it is not easy to flee away with immovable property. Some advantages can be reaped only in a few States of the U.S.A. which do not levy death duties. With the connivance of the decedent, the tax might be evaded. Just before the death of the donor some debts might be concocted in favour of the donee, so that after his death the tax might be avoided to that extent. But where the income-tax authorities are clever and vigilant, such evasions can be detected.

2) *Migration*: Another way by which death duties are evaded is by migrating from one country to another. The nationality cannot easily be changed overnight. Even such a migration may help to evade the tax partly. The change of domicile is in strictest conformity with the legal statutes of the country, as an individual is permitted to change his domicile as and when he chooses. There are several factors to be considered for a change in domicile.

3) *Gifts*. The most common form of evasion and avoidance of death duties is by gifts in contemplation of death, particularly when gift taxes are not levied. These

gifts might be classified into four categories; first, gifts in contemplation of death; second, gifts that take effect after death; third, gift *causa mortis* or death-bed gifts; and fourth, gifts *inter vivos*. Gifts in contemplation of death, are generally subject to death duties. Such gifts have been a dependable factor in the fixation of the rates of death duties. But evasion is possible when any form of these gifts is left untaxed. The taxing authority might prescribe a limit of three to four years before death so that gifts made within the period could be considered as given in contemplation of death. A provision in the statute fixing a time within which gifts would be deemed 'made in contemplation of death', would settle all contention in respect to gifts of this kind. The other remedy will be to follow a supplementary gift tax applicable to all kinds of gifts without taking into consideration the intent of the decedent. The rates too might be adjusted as to differentiate between the gifts in contemplation of death or at the point of death or gifts between living persons. On the face of it, it is quite clear that gifts should be taxed at different rates; particularly those between living persons. As gifts in the last category are not in contemplation of death, any steeply graduated scale can be justified. Surely, a general gift tax would be a valuable addition to the fiscal armoury of the country and if only the taxing authority would do well to be more precise in its basis of gift taxes, the possibility for evasion and avoidance could be reduced to a minimum. The income-tax reports will help administrators of the death tax and evasion or avoidance of gift taxes can be detected without great difficulty.

The community of property of husband and wife in several states with each owning half also contributes in the reduction of death duties as the Federal and the State Taxes apply only to one half of the estate. Both the right of dower and *courtesy* or dower alone, are recognized in every half of the estate and permit a certain amount of death tax reduction in United States of America. These

rights ultimately become effective at marriage. The dower gives the wife a right in her husband's property and the courtesy gives him the right in her property. Both the dower and the courtesy may be wholly exempt, partly exempt, or fully taxed by the State, but they must be included in the estate for the purposes of Federal taxation.

The purchase of life insurance contributes for frequent avoidance of death taxes. Owing to the more liberal exemptions that might be allowed, legal complications do arise in payment of death duties.

Evasion by itself is not a defect in the field of collection of death duties. It is present in every tax. But it can be remedied if the co-operation of the tax-payers is forthcoming and if also the administration is vigilant. "All direct taxation depends very largely for its success on the assent and good feeling of the tax-payer. Apart from illegal or fraudulent evasion, there is always a danger that, if taxation is pressed beyond a certain point, even law-abiding citizens may feel themselves justified in adopting legal methods of avoidance," * said the Report of the Colwyn Committee.

Administration of Death Duties

In the United Kingdom, the Commissioners collect estate duty within six months after the death. They make the allowances of the amount of that duty from the value of the property, in those instances where the property passing on death of the deceased is situated in a foreign country. The Commissioners are given all access to particulars and every information for valuation of property that forms a part of the chargeable estate is put at their disposal. Any person, if he feels that justice has not been meted out to him, can appeal to the High Court within a prescribed time-limit, and the duty then will be payable at the rate fixed by the High Court.

The problem of administration of Death Duties is significant as it stands on an advantageous footing than

* National Debt & Taxation Committee Report, p. 183-184.

any other tax. In United States, its administration varies from one State to another. Assessment and payment are focussed on the executors and administrators of the taxed estates and these persons as officers of the probate courts act in their quasi-official capacity. The activities of these persons are kept under constant vigil, with the result that evasion and avoidance become rare. In some states, the appraisal of the value of the estate does not form the function of the executor or the administrator. The probate courts appoint some "appraisers", while in others the appraisal is done by an agency administering the death duties, or by representatives of the state tax commission, or the chief tax body. Several states designate the chief tax body to serve as the state agency, but the state comptroller, attorney general, treasurer, special inheritance tax commissioner, and auditor are also used in this capacity by one or more states.* But where these duties are administered by probate courts, administration is not what it should be. Where there is the participation of the state comptroller, state treasurer, or the state auditor, some inefficiency is witnessed in administration.

The expenses of collection of estate duties are not much and additional expenses are shared by the estate taxed.

In the Commonwealth of Australia, the Commissioner of Taxation looks after administration of death duties, under the control of the Finance Minister. He is empowered to adopt the state valuations or to make assessments by himself. If the Commissioner finds that an administrator had made some default in furnishing a return, or when he (Commissioner) is not satisfied with the return of the administrator, or when he himself finds some reason to believe that any estate which in his view is not being taxed, he is authorised to assess the property and fix the duty.

In Canada, the authorities seem to be sanguine about the jurisdictional matters. Discriminatory double or multiple taxation might arise there in Death Duties. "It may

* Groves: Financing Government, p. 237.

happen that personal property outside a province, belonging to a decedent domiciled in province 'A' and passing to a resident beneficiary is taxed by province 'A' and also by the jurisdiction (another province or foreign) in which the property is situated. In effect the one tax is levied upon the transmission of the property and the other upon the property itself. A similar duplication may arise between the Dominion and a foreign jurisdiction. . .This form of double taxation is discriminatory in that in the case of two estates of equal size it may affect one seriously and the other not at all, being dependent upon what might be called 'accidents' of domicile and situs". * Here we quote Sec. 7 of the Ontario Succession Duty Act, 1939 as a piece of legislative illustration:

"The Lieutenant-General in Council may provide that where estate, legacy or succession duty is paid in any jurisdiction other than Ontario on property in respect of which duty is levied, an allowance shall be made on account of the payment of such duty, provided that this section shall apply only to such other jurisdiction as makes a similar allowance with respect to the Province of Ontario."

Three decades before the passing of the Act, there existed some reciprocal legislation. Almost every province has similar pieces of legislation. Ontario was ahead in entering into agreements with British Columbia, Nova Scotia, Alberta, Prince Edward Island and New Brunswick, as well as with Great Britain and twenty-six American States, the district of Columbia and the territory of Hawaii. Concessions were later given mutually. Double taxation which is probable in death duties, can thus be avoided.

In most countries of the world, where the estate duty is imposed, the tendency has been to place the administration of the duties in the hands of Tax Commissions. Evasion and avoidance, which are patent in the adminis-

* Succession Duties, Reference Book for Dominion-Provincial Conference on Reconstruction.

tration of death duties, have been reduced to a minimum with the result that the duties have raised the maximum revenue from that source. The productivity of the tax as well as its fiscal justice depends not a little upon the way in which it is administered.

CHAPTER 7

INCIDENCE AND EFFECTS

1. Incidence. 2. Estate & legacy Duties. 3. Incidence of Death Duties in Great Britain. 4. Effects of Estate Duty. 5. Effects on Agricultural Landowner. 6. Effects on Savings & Enterprise. 7. Psychological Effects. 8. Total Effects on Saving & Enterprise. 9. Effects of Legacy and Succession Duties. 10. Effects on Capital. 11. Death Duties consume Capital. 12. Death Duties and Work and Saving. 13. Social Effects of Death Duties.

Incidence

Taxes like income-tax, are paid out of and the burdens are clearly on, incomes. But in the case of death duties, it should be conceived as on capital, payable only at long and irregular intervals. It is "more correct to treat these duties as deferred and accumulated taxes on investment income; they would certainly be taken into account by a reasonable man in assessing the weight of taxation he had to bear." * As death duties are levied on the death of the decedent, the question of incidence, is on a different footing altogether.

The burden of death duties might be looked at from two angles: first, it might fall on the individual's estate at the time of his death, or second, it might be that they are levied at the time of the inheritance of the property. The first occurs in the case of the Estate Duty, while the second in the case of the Inheritance Tax. As the Colwyn Committee remarks in the case of the income tax and indirect taxes, they can be made to conform to *annual* taxes to an individual with a given income in a specified year, on the basis of the schedule of rates in vogue, but in the case of death duties, they have to be related to the same individual in terms of a charge upon his income—a *capital*

* Findlay Shirras and Rostas: The Burden of Taxation, p. 76.

liability, the actual amount of which would ultimately depend upon the wealth, at a very uncertain future date. * The other difficulties are regarding the amount of wealth that might be inherited at the time of the death of the decedent, and the rates that might be in force some years hence.

Let us consider the incidence of death duties, under the two different heads: Estate duty and Inheritance Tax.

Estate Duty

In Estate Duty, as the levy falls upon the property of the deceased, and as it is graduated according to the value of property without any reference to the interests of the beneficiaries, the burden of the estate duty is said to fall on the deceased. The Colwyn Committee explains that "the subject of taxation is, after all, the property which has been held or accumulated by the deceased, and that the tax has fallen upon him, in the sense that it has affected the amount of which he could dispose.. Further, the mere fact that the duty diminishes the property into which the successor may enter is no proof of its incidence being on the successor..."† They went on to say that "on the whole, we think we have good support for giving primary but not exclusive place to the notion that the incidence of the duty is on the predecessor". The same idea was expressed by Sir William Harcourt, the then Chancellor of Exchequer (1894): "The graduated Estate Duty may be, in fact, reckoned in terms of an annual charge upon the estate, and in that shape may be regarded as a graduated Income Tax, which is levied only upon realised property, and does not fall upon what are called 'precarious' incomes. So that, in point of fact, you do arrive at the result which is aimed at in the demand for a graduated Income Tax falling upon what are called 'spontaneous,' as distinguished from 'industrial' incomes."

* Colwyn Committee, p. 79.

† National Debt & Taxation Committee Report, para 456

The other theory puts the incidence upon the successor of the deceased. "Taxes upon the transference of property from the dead to the living", said Adam Smith, "fall finally, as well as immediately, upon the persons to whom the property is transferred". * It is widely held that with the death of the decedent, he will have no rights to the property he previously accumulated and that he consequently is not expected to pay any duty. "The predecessor must be dead before the tax can be levied and dead men, like inanimate objects, can pay no taxes", said Dalton. It is clear that during the life-time of the predecessor he had no tax liability, and might not have at all worried himself about the levy, while the successor who comes into possession of the estate, has no alternative except to pay it. To the extent he pays the levy it can be said that a part of the inherited property has been surrendered to government. This will be more clear when as generations pass by, the successors find that ultimately the whole of the property has been handed over to the public authority. The simple test of incidence of death duties, especially of estate duty, is by withdrawing the duty once, and see who would have been benefitted by the withdrawal and that shows as to who will have to bear the ultimate burden or the incidence of the same. If the duty be abolished the successor will be benefitted, and therefore the tax will be paid by those "who would be benefitted if it were taken off," according to J. S. Mill.

There is the yet another contention that "strictly speaking, the Estate Duty has no personal incidence at all, merely falling upon the estate as such. But it will not be a plausible argument to make an inanimate object assume the place of a man, who has to bear the brunt of the tax, for it is ridiculous to say that an inanimate object, like a house or a piece of land, bears the burden.

If the predecessor, wishing that his successors should not be allowed to bear the duty imposeable on the property that he leaves behind, and if he provides the equivalent

* Wealth of Nations, p. 324.

amount of money for the death duty, it can be easily said that he bears the burden completely. It is true that the testator stripped himself from the hands of the tax-collectors, but because he had set aside the appropriate amount, the incidence is on the predecessor. In this case the testator has to stint himself in his usual expenditure or he would have had to put in greater effort in accumulating the appropriate amount for the payment of the duty, the incidence is on him alone. The desire of the testator in accumulating that sum of money for the payment of tax, depends upon the rate of duties. If the rates are negligible, "the testator would in such circumstances have worked less hard, and the heir would have been no better off. Where, on the other hand, the testator does not curtail his personal expenditure, nor increase his productive efforts, the duties are paid in reality at the expense of the successor". * It might depend upon the attitude of the predecessor as Silverman continues to say: "If the property consists of land or of a business, the testator may be so unwilling to see it broken up that he makes special efforts to accumulate a fund from which the duties can be paid without entrenching upon the main body of the estate. If, on the contrary, the wealth consists of readily saleable and divisible goods, or of stocks and shares, the motive to maintain the estate in an unbroken whole may not be so strong".

Two other theories relate to "insurance method" and "annuity method". In the former case the predecessor takes an insurance policy for paying death duties. Since the value of the policy also forms a part and parcel of total property it should be sufficient to cover duty not only on the value of the insurance policy itself, but also on the original estate as a whole. The Colwyn Committee, therefore assumed that the policy was taken at the age of 45 and also assumed an average rate interest of 5% "in order to translate a given investment income into the principal sum from which it is derived and on which death

* Silverman: Taxation, Its Incidence & Effects, p. 195.

duties are payable". According to Kaldor, "if it is assumed that the owner in each generation saves an annual sum, the accumulated value of which is just sufficient to allow the estate to pass intact to his successor. . . . or, what amounts to the same thing, if he takes out a life insurance policy which is sufficient to cover the total amount of death duties payable, including the increase in the duty due to the policy, and if he does not save otherwise—the net addition to the discounted value of all taxes payable caused by death duties is just equal to the discounted value of the death duties paid; and the annual burden of death duties (if the rate of interest used in discounting is the same as the one at which the savings are accumulated) is just equal to the annual savings. In this case, therefore, but only in this case, the annual burden of death duties can alternatively be looked upon either as the interest on the discounted value of net death duty payments, or the annual savings, made out of income, which provides a 'special fund' out of which death duties are paid".* According to Kaldor the "insurance method" would not give a precise picture of the burden of death duties, for, by saving up for death duties the property owners make their estate liable to pay heavier charges than they would be compelled to pay if savings have not been carried on to that extent. With the increase in the accumulated saving, there is greater estate property to come under the jurisdiction of the taxing authority. Kaldor says: "This is partly because the size of the estate is increased by the accumulated savings; partly also because the more distant death-duty payments, made by successive heirs to the estate, will be on a *constant amount of capital,* instead of on a diminishing amount. The annual burden of death duties, as calculated by the 'insurance method', cannot therefore be regarded as the burden of death duties, applicable in all cases; or, rather, it is only applicable in those cases where estate-owners do,

* Findlay Shirras and Rostas: Burden of British Taxation, p. 82-83.

in fact, save up a sufficient amount to leave their property intact to their successors. It is unlikely that this is the usual practice, especially for the larger estates".†

Because of the several pitfalls in the insurance method in the determination of the burden of death duties, Mr. Kaldor developed what can be called "an annuity method". It involves an estimate of what the net income from property would be if there will not be death duties, and a similar estimate of what the net income from property would be if there will be death duties. In the former case there would be no fluctuation in the net income, while in the latter, the net income would dwindle with succeeding generations, "but the net income will not be diminished in the same proportion, since the percentage of the smaller gross income taken in income taxation will be lower". The burden of death duties can be ascertained by calculating the size of the income stream, and finding out the present capital value of the estate and then the difference between the present capital value of the estate and this discounted present value of future income represents the burden on the *capital* of the death duties, and the interest on this sum represents the burden on income.

Legacy and Succession Duties

In the case of the legacy and succession duties, the problem is not so complicated as it was with estate duty. Where the property is inherited by a direct heir, the rate would be naturally smaller than otherwise. If the testator or the legator undertakes to appropriate a sum to cover the payment of the levy, the incidence would naturally rest on the testator or the legator; but in those cases where the testator or the legator do not have any interest to accumulate, being not in the direct line of descent perhaps, the beneficiaries or successors will have to bear the burden of the legacy or succession duties. The Colwyn Committee Report embodied: "These minor duties are

† Findlay Shirras and Rostas: Burden of British Taxation, p. 83.

in the nature of acquisition duties on the beneficiary. A testator who looks forward to leaving his property to his wife or children, and who sets himself to work harder or to save more in order to provide for payment of Estate Duty, is likely also to take these duties into account (the rate payable where property passes in direct line is only 2%). He is less likely to attempt to make provision as regards any property going to a brother or sister (in which case the rate would be 5%), or to a cousin or friend (in which case the rate would be 10%). The main yield of the duties is from the 5% and 10% rates....The intention is that the duties should fall upon the person receiving the benefit, and we think that, in fact also, the burden should generally be regarded as falling upon him". As it is from the higher rates that the greatest part of the revenue is realised, it can be maintained without any doubt that the general incidence of these minor duties is on the beneficiaries.

The minor duties are very much akin to the estate duty, and to be more precise, treated as additions to the estate duty. Minor duties are paid by the beneficiaries, whereas the estate duties are paid by the estate, that is, "the legator by legal fiction".

Incidence of Death Duties in Great Britain

According to Dymond, the estate duty in Great Britain is considered as a testamentary expense in respect of the free personal estate of the deceased. The duty will be paid from out of the estate. In the absence of any declaration in the will, the estate duty will be paid primarily out of the lapsed shares, the burden falling wholly on the legatee ultimately. "Except as regards the free personal estate of the deceased in Great Britain, and subject always to any direction in the will or disposition, it is an almost universal rule that every beneficiary bears the estate duty attributable to the property which he takes". * In that case the estate duty will be deemed as one imposed on the property and will not be regarded

* R. Dymond: Death Duties, p. 141.

as a testamentary expense. If the beneficiary receives real property according to the directions in the will, the duty will be wholly upon him, but in case estate duty is a charge on all the beneficiaries it will be borne by all, who become entitled to the actual property or to any benefits. For example, Dymond says, that a widow entitled to terce, bears a proportionate part of the duty on her husband's heritable estate. The same principle also holds good as between pecuniary and residuary legatees, and as between the persons entitled respectively to a rent charge or portion and the settled property subject thereto. * In a case where an estate duty is imposed upon an annuitant, he should be treated as tenant for life of a "slice" of the property sufficient to produce his annuity, and be required merely to pay interest on the duty attributable to that "slice"..the duty itself being paid out of the corpus of the property. † It was illustrated as follows: For example, an estate worth £6,000 and producing £240 per annum, was settled on *A* for life. On his death an annuity of £50 was charged thereon in favour of *B* and subject thereto the property passed to *C*. Estate Duty is payable by *C* at (say) 5%, without deduction for the annuity. The "slice" of the property required to produce the annuity is $50|240 \times 6{,}000 = 1{,}250$, and the relative Estate Duty is £62 10s. *B*, however, is entitled only to the income of the "slice", and can therefore be charged only with interest on the duty. The result is that *C* may deduct, from the £50 per annum, interest on £62 10s. If the duty has been raised by mortgage, the rate of interest is that payable under the mortgage. If not, the rate is that at which a mortgage could be raised. In cases, where the annuity is taxed directly, the beneficiaries would naturally pay the levy. But in very extra-ordinary circumstances, as Dymond points out, "where the property passing was the benefit of a direction to pay out of the income of the testator's residuary estate, the out-goings, etc, in respect

* R. Daymond: Death Duties, p. 143.
† Ibid, p. 146.

of a house and its contents, which were given to *A* for life, then to *B* for life, then on other trusts, the court ordered that the duty in connection with the death of *A* on the benefit of the direction (not the duty on the house and contents) be paid out of the residuary estate and be recouped by means of a policy on the life of *B*: and that interest on the duty and the premiums on the policy be retained by the trustees out of the annual sum which would otherwise be payable under the direction". *

The provisions in a will or other disposition which specify particulars about the incidence of estate duty fall into these categories according to Dymond: directions that duty should be paid *en bloc* from a particular source, and direction that specific property, which would ordinarily bear its own burden should be free from duty. The first category includes the estate duty on personal estate of the decedent, wherein it relates to "testamentary expenses", that is those duties to which the estate is liable by reason of the dispositions in the testator's will. But a pecuniary legacy payable out of the testator's personal estate which is "subject to any duty thereon" or "subject to death duties" is not "required to bear any part of the estate duties in connection with the testator's death, but if it is settled it bears its own duty on the death of a life tenant".

Effects of Death Duties

The Colwyn Committee has mentioned some of the most interesting effects of death duties:

Private Business. It has been maintained that public limited companies are not so much directly affected by the imposition of death duties as private businesses. In the former case, as they are limited companies, the death of any share-holder will not have any effect on its structure as a whole, whereas private concerns, financed by rich individuals, will have to be broken up at the death of one of the partners.

* R. Dymond: Death Duties, p. 147.

Private business will naturally be affected to a great extent by death duties. The Association of British Chambers observed that "death duties dispute and divert capital from business channels often at a critical moment in the life of a concern, and make serious inroads on the credit of those affected". The National Chamber of Trade stated that "businesses and undertakings passing at death from father to son in quick succession have in some cases been seriously crippled, and have actually ceased to be sources of income at all." Lord Forrest found it plain that the death duties affect private business very seriously and much more so than companies. It has now become a risky matter to have too rich a partner. Death is uncertain and may come unexpected, and at the most inconvenient and embarrassing moment for the firm. However considerate the provisions of a deceased partner's will may be, and even if he had a son to succeed him in the business and become entitled to a portion of his means, the demands of the Inland Revenue must be met, usually from liquid resources employed in the firm, and in the case of a large fortune, are so heavy as to upset and in some cases to embarrass the business". Sir Felix Schuster said: "The duties can in most cases only be paid through bankers' advances, which take a long time to repay, and the effect on the business must necessarily be very serious and hamper its work and development". It cannot be denied that any form of death duties will have its embarrassment and serious effects on private businesses, but the seriousness of the effects will depend largely upon the frequency of the cases under consideration. It was proposed by McKenna that "the number of large private businesses likely to be involved heavily by death duties is small." Particularly, when exemption has been put at a high level, it is quite obvious that a small number of private businesses will be taxed more steeply than in other cases, and as such the extent of the damage depends upon the value of the estate. Many witnesses before the Colwyn Committee argued that the tendency of death duties to bring about conversion of private concerns into

public companies will not bring about any extinction of the business itself. But Dr. Dalton advocated "in favour of anything which accelerates the transformation". This would also be in comformity with the socialistic principle of encouraging public companies rather than private ones.

Effects on Agriculture

The plight of the agricultural landowner received the attention it deserved from the Colwyn Committee, through the representations it had from the Central Land-Owners' Association, the Land Agents' Society and the Land Union. The general view of the agricultural landowners is that the expenditure involved by a large agricultural estate in the payment of death duties is very heavy. The death duties would break up landed estate, contribute more expenditure and lessen eventually employment of agricultural labour.

The Central Land Owners' Association argued that death duties "press with exceptional severity upon agricultural land, because it has a market value relatively far in excess of its income-producing value, and also by reason of the basis of valuation adopted in practice". It was suggested that agricultural estate should be valued on a fair capitalization of annual value in the imposition of death duties. The force of that argument cannot be denied, though as Mr. Pretyman said: "Say you buy a farm in the Fens, that has got absolutely no amenity at all; it is purely an investment. But if you buy a pretty poor land in the southern countries, with a nice house on it and some woodlands, and an attractive view, that is all amenity as much as a picture". Thus, the Colwyn Committee says that the root principle of the estate duty is that it is levied on the value of capital assets, whether it yields money income or not.

The Scottish Land and Property Federation favoured elimination of amenity value and maintained that the transfer of the landed estate was "the annihilation of the tenancy system, under which the farmers of this country have been unable to devote their whole capital to their far-

ming operations instead of locking up more than half of it in the land and equipment which are required therefor". More has been stated in favour of the agricultural landowner that in regard to agricultural land. The landowners have had singularly few opportunities as compared with other members of the community with equal wealth, of saving out of income for the purpose of meeting death duties.

Psychological Effects

The Colwyn Committee have discussed the psychological effects of death duties. They have posed for themselves two questions: whether the estate duty will stimulate the tax payers to work and save and whether it will discourage them from working and savings. While comparing the income tax and the estate duty, the majority report of the Committee was of the opinion that the income-tax will cut short consumption even of the most improvident man in his attempt to meet the same, while the estate duty which is a tax that the person in present enjoyment of the estate can ignore, is naturally liable to make the tax payer sanguine in view of his life expectations to ignore the psychological effects altogether. Sir Felix Schuster considered the estate duty "especially injurious because it falls on future generations and to a greater extent the present is inclined to disregard its consequences". The view of Professor Pigou is that "death duties are rather a good form of taxation, in that people are probably not discouraged from saving by thinking of the death duties as they are by thinking of an Income Tax on an unearned income." Dalton too hoped that death duties will not discourage savings any more than an income tax, and "on the other hand, the prospect of heavy death duties will stimulate those who are waiting for a windfall of inherited wealth to work harder and to save more than they would otherwise do". Death duties which fall only on unearned increments or windfall wealth which are not expected, are liable to reduce effects on work as well as desire to save. In defence of death duties, Prof. Macgregor stated: "It is also to be noted that the

purpose of savings is not only to provide for posterity, but also to maintain and increase the personal standards of life, power and reputation of those who save; death duties miss these motives, while any form of alternative taxation will, to some extent, hit them".

Total Effects on Saving and Enterprise

Because of its physical and psychological effects, the estate duty has been found to be damaging to saving. But does it necessarily mean that the total effects on saving and enterprise are more damaging than a substituted income tax, particularly "if that tax were confined to income corresponding with the capital on which estate duty is paid." The Colwyn Committee reported: "Under the yearly tax, those who live wholly or mainly on investment income might, on balance, be stimulated (in some cases even physically compelled) to effect some extra economies. On the other hand, the differentiation against income from savings as compared with earned income would be more obvious in an yearly tax than in a tax deferred till death. It seems probable, therefore, that, to some extent, it would tell against saving out of earned income. In the larger estates, the burden would be a serious addition to the income tax and supertax, and would be more depressing than the prospect of estate duty at the uncertain date of death. Altogether, we think that, in conjunction with the ordinary income tax and supertax at their present level, the estate duty is decidedly less damaging to saving and enterprise than a corresponding yearly tax would be.... In so far, then, as the object of the Estate Duty is to differentiate against accumulated wealth, it can do so in a manner less prejudicial than a special Income Tax covering the same field". *

Legacy and Succession Duties

There are some minor duties which serve as complementary to the major estate duty. These can be looked at as acquisition duties based on the assumption that a person

* Colwyn Committee Report, p. 194.

who is a legatee or a beneficiary will be liable to pay this tax. There is much similarity between the estate duty and the other minor death duties. If the beneficiary happens to be the direct descendant of the decedent, he pays a lower rate than that which a collateral heir or a distant beneficiary would pay. The estate duty is to be paid on the estate without any relationship discrimination; but in levying legacy and succession duties relationship discrimination and other exemptions exist. The legacy and the succession duties form the whole basis of death duties, either from the point of view of productivity or from the justifiability of the tax imposed. They serve only as a complementary force taking into consideration the ability of the successor or the beneficiary to pay the taxes.

Effects on Capital

Death duties are not the only taxes that fall on capital. Taxes on property which are levied periodically are as good as taxes levied against the value of property; license taxes, sales taxes, income tax etc., have also to be paid out of capital rather than out of income at times. The ultimate taxes of death duties are determined largely by the effects of standing of the revenues derived from that source. Sir Josiah Stamp was of the opinion that the influence of death duties upon saving is only slightly unfavourable as compared with the other taxes, and that their desirable and social effects must likely counter-balance any disadvantages to capital accumulation. Apart from other economic effects, he is of the opinion that the current expenditure of tax collections by Government is liable in all probability to add more to the nation's power of accumulation than the capital, when the capital taken from individuals by inheritance taxation". *

Death Duties Consume Capital

That death duties consume capital by itself is one of the most important apprehensions of the critics. The argument is that death duties dissipate the capital of the

* Sir Josiah Stamp: The Fundamental Principles of Taxation, p. 157-69.

nation and thereby lessen the amount necessary for the industrial development. Wealth that might have been utilised for industrial purposes might now be diverted to the Treasury. To that extent the national capital might be diverted but not dissipated. The state might be promoting several industrial concerns, or it might be meeting the irrigational and other developmental expenditure. Only in those cases, where the state has no specific policy of expenditure or where it does not spend for nation-building activities, but utilizes it for war-purposes, can it be said that the capital is being dissipated. Death duties will not be at a disadvantage particularly when a comparison is made between them and the income tax. Where income tax falls on potential capital, it can be argued that the national capital is being destroyed. Moreover, the income tax falls on more persons than the death duties. The latter affect only some medium-sized and large estates. Groves argued thus: "Take the case of three people, each with a $4,000 income. *A* lives from hand to mouth. His income-tax means reduced consumption for him. He pays no inheritance tax when he dies. *B* is very prudent and will provide his dependents with a certain standard of security regardless of taxes. Both his income tax and his anticipated death taxes will come out of his living. Since he saves in anticipation of death taxes, it may seem that until the occasion arises to pay them, savings are positively augmented by the existence of the death tax. This is true individually, but not collectively, since *B*'s extra savings are needed to buy the capital of someone else whose estate is now paying its death taxes. *C* is moderately prudent, but he has a rigid scale of living. Each year he saves all and only what he earns above $3,500, which means that whether income or death taxes, as contrasted with death taxes, reaches many like *A* who have no inclination to save, it tends to reduce accumulation less than the death taxes. On the other hand, death taxes tend to discourage the propensity to save less than income taxes because they do not weaken the saving habits of the tax payers. This is true because of their remoteness and

the lesser interest which one naturally has in what happens after death. On the whole, one should probably say that the death taxes discourage capital accumulation somewhat more than income taxes, dollar for dollar, but the difference between the two in this respect is not a great one". * Thus the income tax and the death duties might almost have the same effects on capital. But it can be conceived that the institution of inheritance could be abolished without the destruction of capital, though it should be made clear that it is not very difficult to dissipate and get destroyed national capital by pursuing a confiscatory system of death duties. So the capital accumulation or destruction depends largely upon the rate of death duties and other factors.

Death Duties and Work and Saving

There are two schools of thought, the former, represented by Sir Felix Schuster, considers that death duties are bad enough as they are forgotten by the living who have no inducement to make any effort to provide for them by extra saving. The second school of thought maintains that these duties are a great obstacle to "found a family" and that much attention cannot be bestowed on accumulating sufficient property for the heirs. In other words, the estate owners would not like to leave behind property for their descendants, for fear of paying the death duties. Others like Bertrand Russell argue that "ordinary work is done for the sake of a living and the best work is done for the interest of the work itself". There might be a few who accumulate property, being actuated by the sense of social security. The death duties therefore will not have any adverse effects on the ability to work and save.

The motives prompting human activities can be analysed as follows: firstly, to provide for future expenditure saving is done. It can be called as Sir Josiah Stamp puts it, "long distance spending". The savings of the labouring population can be a case in point here, and as

* H. M. Groves: Financing Government, p. 233.

the saved-up money has to be ultimately utilized for one or the other purpose, and as the amount involved will be small, the effects of death duties on it will have little effect on saving and working. The middle classes' saving is effected to obtain or increase income from investment. "An inheritance tax cannot affect the force of this motive except in so far as it cuts down incomes from inherited property and thus makes the getting of additional investment income more desirable". Thirdly, those rich men without big families go on accumulating as the wealth that they command gives them social distinction and position. They might be imbued with the love of accumulating—accumulating for its own sake. It is therefore doubtful whether death duties will have any remarkable repercussions on work and saving. Fourthly, the rich save in the hope that after death, their nearest and dearest successors will not be put to any inconvenience. Provision would be made by the parents usually out of affection for their children or other direct heirs. The parents think it to be their duty to accumulate property with that end in view. Death duties under the circumstances do not affect the motives of the parents, or affect their work and saving.

If the rich are to be taxed with the minimum disincentives to production and the minimum loss to saving, the most important venue is death duties. Dr. Dalton, in his evidence before the Colwyn Committee put forward his case thus: Death Duties are "a source of revenue which should be considerably developed. Inherited wealth is wholly unearned and, in excess of a moderate amount it encourages idleness and thriftlessness in its recipients. It is therefore, a peculiarly appropriate object of taxation I believe that the anticipation of posthumous payment of death duties discourages work and saving to a much slighter extent than the anticipation of recurrent payments of income tax on this side of the grave. On the other hand, the prospect of heavy death duties will stimulate those who are waiting for a windfall of inherited wealth to work harder and save more than they would otherwise do".

Social Effects of Death Duties

Apart from the economic affects the social effects of death duties are equally important and significant.

The main idea in the imposition of death duties is to bring about an equalisation of wealth. This is one of the most conspicuous social considerations in levying of death taxes. Increasing frequency of death duties was defended on the basis that it tends to reduce inequality of wealth and stem the growth of heriditary plutocracy and "certainly this social consideration has been as important a motivation of the high progressive rates of the federal estate tax as any fiscal consideration". Prof. Seligman having posed for himself the question as to why democracy should favour these taxes reconciles himself by saying that "the trend of democracy is necessarily towards socialism, the answer is plain: the inheritance tax is imposed because democracy is jealous of large fortunes". Equality can be achieved by stopping the transmissions of large amounts of property at the death of the decedent. The rich that leave behind large estates to their sons, introduce inequality in the general distribution of wealth and income, and unless and until the stream of property is not diverted, inequality would be on the increase. Death duties form a highly effective weapon in bringing about equalisation of wealth and income, and the consequent social effects would naturally be very congenial to the growth of industry and the feeling that there is no gulf between the haves and the have-nots gives more incentive to the labouring classes to speed up production.

Direct social effects would also accrue and they depend on the earmarking of the revenue. In the past the revenue derived from death duties was earmarked for the maintenance and support of the educational or charitable institutions. Several continental writers argued that the revenue should be earmarked for capital expenditure, that is for educational and charitable purposes, rather than for general expenditure. They were of the opinion that the revenue could be expended for maintenance of hospitals and the establishment of sickness

insurance. * Rignano advocated duties with a view to bringing about state socialism one day or another, or rather he wanted that the revenue yielded by the death duties should assume the form of corporate securities and other deeds to capital wealth. †

The social effects of death duties would naturally depend on the different aspects of expenditure. In most countries, the death duties are being levied by the provinces and they are utilising this for the development of the economy by executing the post-war schemes or for social expenditure. Generally most of the revenue is earmarked for social services. Thus the social effects would be most salutary, and the imposition of death duties is therefore doubly justified.

* Shultz : The Taxation of Inheritance, p. 330.
† Social Significance of the Inheritance Tax, Pt. II. ch. 2.

CHAPTER 8

INTRODUCTION OF DEATH DUTIES

"Death Duties on graduated scale shall be levied on property above a fixed minimum."

—Resolution at Indian National Congress (Karachi 1931)

1. Laws of Inheritance. 2. Hindu Law. 3. Muslim Law. 4. Constitutional Position of Estate Duties. 5. Succession or Estate Duty. 6. Objects of Estate Duty Bill, 1948. 7. Hindu Code and Estate Duty Bill. 8. Important Sections of Estate Duty Bill.

Laws of Inheritance

Hindu Law

From 1914 onwards, there have been many Acts bringing about marked changes in the Hindu Law, the earliest of them being the Hindu Disposition of Property Acts. Then there were some Acts affecting the Mitakshara Law of Inheritance. The Hindu Women's Rights to Property Act, 1937 (as amended in 1938) was designed to make the widow a co-heir or co-parcenary in the property along with her sons. That would give her a place in inheritance of property.

Later, in 1941, the Government of India referred the whole question of amendments to Hindu Law to a committee which proposed to bring about into a code "all the subjects on which the Centre can legislate at present, viz. testamentary and inter-state succession (including maintenance), marriage and divorce, minority and guardianship, adoption."

The Bill to amend and codify certain branches of the Hindu Law which was referred to a Select Committee recently, brings about some desirable changes in the laws of inheritance of the country.

There are two schools under the Hindu Code—Mitakshara and Dayabhaga. According to Mitakshara,

the property of a Hindu is not his individual property, but it belongs to what is called a co-parcenary which consists of father, son, grandson and great grandson. All these persons have a birthright in that property and it passes on by survivorship, to those persons who remain after the death of the decedent and does not pass on to the heirs of the decedent. Under the Dayabhaga, the property is held by the heir as his personal property and he has an absolute right to dispose it off either by way of gift or by will or by any other manner. "On the death of the father, the son takes the property not as his heir but by survivorship." * Here, the co-parcenaries in a Hindu joint family do not possess any right as individuals. That is why a Hindu joint family is considered as a "corporate family having a continuous existence, notwithstanding the death of individual members." † Under Dayabhaga, the sons do not take any interest in their ancestral property during the lifetime of their father, and it is only after his death that they acquire the interest; but under Mitakshara the sons acquire an interest by birth. The difference between Mitakshara and Dayabhaga is shown by the following illustration: *A* is a member of the Hindu joint family, which is governed by the Mitakshara Law of Inheritance, who dies leaving five sons and a property worth Rs. one lakh. The tax on it will be one-sixth of Rs. one lakh, because *A*'s share would also have been there before the partition of property took place and his son, not being his successor but co-parcener, will not be entitled to the share of *A*'s property. But *B*, also a Hindu, when governed by the Dayabhaga Law of Inheritance, dies leaving five surviving heirs, the inheritance tax on his estate valued at Rs. one lakh, will be six times that of the amount which *A* paid.

The Bill to amend and codify the Hindu Law proposes important changes. Firstly, the widow, the daughter, the widow of a pre-deceased son are all given the same

* D. F. Mulla: Principles of Hindu Law (1936), p. 323.
† Sir E. J. Trevelyan: Hindu Law as Administered in British India 1939, p. 213.

rank as the son in the matter of inheritance. The daughter too is given a share in a father's property which is prescribed as one half of the share that comes to the son. The rights of other heirs of the family have already been recognised under the Hindu Women's Rights to Property Act of 1937. Secondly, the number of family heirs according to the Bill, is much larger than those under Mitakshara or Dayabhaga. Thirdly, where under Mitakshara or Dayabhaga, a discrimination has been made amongst the family heirs on the ground of the economic status at the death of the testator, whether a daughter is married or unmarried, whether she has any issues or none, such palpable discriminations under the older laws of inheritance, will be removed with the passing of this Bill.

"On the subject of the joint family system under the Mitakshara Law and the many different laws of inheritance in India, the Committee (The Taxation Enquiry Committee), as laymen, speak with diffidence. They are advised, however, that these two conditions generally put an acquisition duty on the lines of the English succession and legacy duties out of question. The joint family is in the nature of a corporation which continues to exist and enjoy the property irrespective of the death of any particular member. Meanwhile, the systems of inheritance, both among the Hindus and among the Muhammadans, recognise a plurality of heirs, and the calculations connected with the division of property among them, and more particularly the minute fractions into which the shares of particular heirs may run, would render the imposition of a succession duty, as distinguished from an estate duty, impracticable. Nor would it be easy, in the medley of laws and customs of inheritance that exist side by side, to arrive at uniform classification of heirs and a satisfactory scale of graduation according to the relationship which would apply to all communities in India. For these reasons also, a duty somewhat on the lines of the English estate duty appears to be more practicable, and may initially take the form of a transfer or mutation duty on death.".*

* Taxation Enquiry Committee Report, p. 264.

In Malabar there prevails the *Tarawad* system, under which the individual members cannot have as of right any claim to partition of the *Tarawad* property, nor any right of testation. The Indian Taxation Enquiry Committee referred to this peculiar system as one that is quite conspicuous in that the right of an individual member thereby to demand or enforce a partition is not recognised and that there can never be a partition. It would therefore be impossible to tax the undivided interest in the *Tarawad* property in the absence of any right to demand partition. This makes it very difficult for the estate duty to be levied without bringing about a complete revolution which might amount to a negation of the law itself. The only alternative that struck the Taxation Enquiry Committee as regards the property belonging to such a body is to levy, instead of an inheritance tax, an annual tax in the nature of a corporation tax, the minimum limit of exemption being dependent on the number of people supported by the *Tarawad*.

Muslim Law

All the Muslims have been divided into two sects; Sunnis and Shias. Among the Sunnis, there are four sub-sects, the great majority of them belonging to the *Hanafi* school; while the Shias are divided into three sub-sects. Then again the law applicable to each school varies from one to another. In the case of Shias and Sunnis, inheritance of property of the deceased is governed by the respective law of the corresponding sect to which he belonged, and not by the law of the sect to which persons claiming the property as his heirs belong. In those cases where property has to be inherited from a Muslim dying intestate in specific shares on the occasion of his death, the successors taking their shares severally will be analogous to those of tenants-in-common, which means that the Muslim Law is based on the principle of legitim rather than the joint ownership or survivorship as in the case of Hindus. Moreover, the Muslim Law makes no distinction whatsoever in the matter of the inheritance of ancestral and self-acquired property or movable and immovable property. This complicates

the whole issue of the imposition of estate duty as it has to be based on a broad distinction between self-acquired and ancestral property as naturally as the amount of property that would be inherited should be taxed more heavily than the property that has been accumulated as a result of personal labour.

Unlike in the case of the Hindu Law, the Muslim Law does not recognise the right of a heir-apparent or presumptive till the death of the predecessor.

The Muslim Law recognises different classes of heirs in the matter of the distribution of the estate: 1) Sharers; 2) Residuaries; and 3) distant kindred in the case of Sunni Law; and sharers and residuaries in the case of the Shia Law. According to the Shariat, the shares are specifically laid down in fractions and the actual division among the multiplicity of recognised heirs is quite complicated. It is accepted that the Muslim is entitled to make a bequest of one-third of the estate and even more with the consent of his heirs. There is also a special recognition of the right of gift to the extent of one-third of his estate before the death, during 'marz-ul-maut' or death illness.

Constitutional Position of Estate Duties

The Government of India Act, 1935, envisages a system of death duties. It provided for legislation regarding duties on succession of property, as distinct from estate duty. The Act provided that duties in respect of succession to agricultural land shall be levied and collected by the provinces. * In respect of duties of succession other than on agricultural land, the Act embodies that such duties should be levied and collected by the Federation but that the proceeds of the same would be distributed among the provinces. † The Government of India had to consult the Federal Court regarding their bona fides in levying death duties, but a negative reply was given by the Federal Court. It gave majority ruling that it did not fall within the ambit of the Federal Legislative List. That is the

* Provincial Legislative List, Item 43.
† Federal Legislative List, item 56.

reason why the Central legislation could be taken only with a view to levy an estate duty on non-agricultural property, while at the same time the provincial Governments are entitled to the proceeds of the estate duty. The Act which in the beginning, according to the opinion of the Federal Court, did not empower the Central Government to impose death duties, was, therefore, later on, amended in respect of non-agricultural land or property.

The Taxation Enquiry Committee suggested the imposition of the inheritance tax as early as the years 1924-25 with a view to removing the inequalities in the distribution of wealth and incomes. Mr. Layton's report to the Indian Statutory Commission in 1930 was also in favour of a system of death duties. It was stated that "in India death duties might take the place of income-tax as a means of imposing a graduated partition on agricultural incomes. A probate duty already exists in certain areas but it is limited to particular communities and the rate is low. The possibility of imposing death duties throughout India has been exhaustively considered by the Indian Taxation Enquiry Committee, and the question has also been discussed by the Government of India with the provincial governments. On political and legal difficulties in the way of the imposition of this tax which arise mainly from the complexities of the Hindu Law of Inheritance, I am not competent to express any opinion. In most federations death duties are wholly assigned to the constituent states or provinces, but general taxation for the regulation of taxes has been found necessary in some countries in order to avoid double taxation.....The tax if levied in India, would therefore probably have to be administered by a central authority and distributed among the provinces."

In the report of the Federal Finance Committee, better known as the Percy Committee (1932), "Taxes on land, including death or succession duties in respect of succession to land" were put under the head 'Sources of Revenue Reserved to the Units'.

The "Proposals for Indian Constitutional Reform", better known as the White Paper (1933) in Section 138, embodied the following:

Duties on property passing on death (other than land).
Taxes on mineral rights and on personal capital (other than land).
Terminal taxes on railway, water or air-borne goods and passengers, and taxes on railway tickets and goods freights.
Stamp duties which are the subject of legislation by the Indian Legislature at the date of federation.

"The net revenues derived from the sources specified in the margin will be assigned to the Governors' Provinces. The Federal Legislature will, in each case, lay down the basis of distribution among the Provinces, but will be empowered to impose and retain a surcharge on such taxes for Federal purposes."

Succession or Estate Duty

After considering the laws of the land regarding inheritance it is certain that the imposition of an Estate Duty rather than a Succession Duty would be justified. In fact both would be complementary to each other. The Taxation Enquiry Committee in their report summarised their ideas thus: "On the subject of the joint family system under the Mitakshara law and the many different laws of inheritance in India, the Committee, as laymen, speak with diffidence. They are advised, however, that these two conditions generally put an acquisition duty on the lines of the English succession and legacy duties out of question. The joint family is in the nature of a corporation which continues to exist and enjoy the property irrespective of the death of any particular member. Meanwhile, the systems of inheritance both among the Hindus and among the Muhammadans, recognise a plurality of heirs, and the calculations connected with the division of property among them, and more particularly the minute fractions into which the shares of particular heirs may run, would render the imposition of a succession duty, as distinguished from an estate duty, impracticable. Nor would it be easy, in the medley

of laws and customs of inheritance, that exist side by side, to arrive at a uniform classification of heirs and a satisfactory scale of graduation according to relationship which would apply to all communities in India. For these reasons also, a duty somewhat on the lines of the English estate duty appears to be more practicable, and may initially take the form of a transfer or mutation duty on death." *

The joint family system is so potent, because of the prevalence of the rule that the sons by birth become naturally the coparceners and claim equal right to the estate or property. So long as their father lives, the property will not be partitioned, and even that property that they are entitled to get, is only the share of the family property which they could have obtained at the hands of the father. The tax could be so imposed as to fall only on the share that he obtained and not on the entire estate. This is legally speaking the correct argument. But if this is made the real instrument on which the fiscal liability is supposed to be based, there would be a great discrimination and consequently fiscal injustice, as a result of the right of bequest, etc. Moreover, in a poor country like India, where the individual shares of property are bound to be too meagre, the administration of the tax may become difficult and costly. The laws of inheritance and the administrative difficulties peculiar to India necessitate the imposition of an estate duty on the lines of the one in Great Britain, rather than the Succession duty.

Recently, the Indian commercial community has has come to prefer a succession duty to an estate duty, because the former would be in consonance with the existing laws of inheritance in the country. It was also suggested that in a joint family, the share of each surviving co-partner might be subjected to a succession duty separately, while under the Estate Duty Bill, the whole of the joint family property would be the basis of the estate duty. It is in this light that some thinkers began to recapitulate what the Finance Minister had stated in the Budget Session of the Legislature that the Government would be prepared not

* Taxation Enquiry Committee Report, p. 264.

only to consider improvements in the existing draft but also an alternative measure converting it into a succession duty. Some time ago, the Federation of Chambers of Commerce and Industry has represented to the Finance Minister that theoretically the succession duty would be more easily brought into effect; but has at the same time pointed out that the measure should not be effective until the return of normal conditions. It also emphasised that apart from the general economic deterioration, the rapid pace of social legislation introduced by the Central and the Provincial governments has put a heavy drain on capital, and the introduction of the measure will aggravate the shortage of capital for industrial development.

With the disruption of the joint Hindu family and the recognition of the rights of the Hindu widow and daughter to equal estate of a deceased dying intestate would constitute difficulties in the imposition and collection of the estate duty. But on the other hand the abolition of the joint Hindu property and the denial of right to property by survivorship will indeed simplify the process of collection of the estate duties from those Hindus dying intestate, for if the estate left by the father is liable to duty, his heirs will have to naturally pay according to the estate duty act. "That portion of the bill which relates to the taxation of Hindu undivided families, levies the charge on a benefit or interest ceasing at the time of the assessee's death. At this time, the interest of the deceased is certainly capable of being fixed precisely and definitely. To the extent that what the deceased expected to inherit, which will be hit by the tax, differs from what is subsequently determined, on the basis of precise and ascertained facts as the deceased's share on that date, an injustice of some kind may arise. . ."

According to the Estate Duty Bill, 1948, therefore a duty will be levied which will be not of the mere *succession* type, as the word is understood by the English jurists. Succession duty, in other words, is one that is imposed upon the individual shares of the deceased's estate, either an intestacy or by will or by any other instrument for the disposition of the estate or property, at the time of the death

of the deceased. But the estate duty is a levy on the entire estate as a whole. That the estate duty is more productive and that it satisfies all the canons of taxation has already been shown.

When the question regarding the competency of the Federal Legislature in enacting the estate duty bill arose in 1944, the Governor-General referred the same to the Federal Court, and then there was a great controversy about the distinction between "Estate Duty" and "Succession Duty". In the judgment it was said that "though economists and writers have dealt with Succession Duty and Estate Duty under the headings Death Duties, Inheritance Taxes and Duties on Succession, it cannot be said that they did not recognise a real distinction between Succession Duty and Estate Duty. There are certain common features justifying the treatment of both these methods of taxation under one head; but the distinctive features are also noted. Thus, Findlay Shirras in his *Science of Public Finance* (p. 524) classifies Death Duties or Inheritance Taxes

> 'under two categories, an estate tax levied on the inheritance as a whole, and a succession duty or share tax on the separate portions going to the different beneficiaries.'

He adds that both categories have their peculiar characteristics and proceeds to indicate them observing that the Estate Duty is a more productive and efficient source of revenue while the Inheritance Tax may be said to be the more equitable. There is one feature common to both taxes, namely, that the occasion for the levy is the death of a person; but while Succession Duty has reference to the acquisition of the property by the successor and generally takes into account the extent of the benefit derived by him and other considerations relevant from that point of view, the Estate Duty has reference to the value of the property constituting the estate of the deceased and is independent of the question as to who takes it. Thus the distinction drawn in the English decisions between Estate Duty and Succession Duty seems to correspond substantially to a distinction in principle and basis recognised by writers on

Economics." (*Vide* Judgment of the Federal Court in A.I.R. 1944, F.C. Page 73 at page 77).

Objects of Estate Duty Bill, 1948

The Estate Duty Bill has been on the anvil since a pretty long time. Sir Jeremy Raisman concluding his budget speech of 1944-45, expressed that the Government have "under active consideration the possibility of an estate duty on non-agricultural property, which would be assigned to the Provinces. In spite of war-time taxation it is indisputable that enormous private fortunes have been made during the war aggravating the great inequality which already existed. Even on a modest programme vast sums will be needed for the post-war development of the country and there is manifest justification of a system of death duties, whereby these large fortunes will be laid under contribution. I have no doubt that such a measure would not only fill a gap in the fiscal armoury of India but could serve a great social end." The influence of these words was seen in Sir Archibald Rowlands' introduction of the Bill in 1946. Later in 1947, before the constitutional developments took place it was moved by Mr. Liaquat Ali Khan, and afterwards in 1948 was introduced by Sir Shanmukham Chetty.

The main objects of the Estate Duty Bill, according to the 'Statement of Objects and Reasons' embodied therein are: Firstly, "to assist the Provinces to finance their development schemes by fortifying permanently their revenues and enabling them to improve *inter alia* the existing social services"; and secondly, "In spite of war-time taxation, enormous private fortunes have been made during the war, aggravating the great inequality which already existed.... It will be a step in the process of reducing the great disparities of wealth, which is a prominent feature of Indian economy, and will set the country moving towards a more equitable distribution of the national income".

This measure is mainly intended for affording the Provinces a permanent revenue, so that they may be

able to carry on their post-war reconstruction and development with the necessary financial strength. Estate duty in respect of property other than agricultural land and that of succession to property would be, according to the Bill, levied by the Centre or by the future Indian Union, and the proceeds of the same would be distributed among the units of the Federation of the Union. It is thought that the Estate Duty will provide a perennial source of revenue to the provinces, and as according to the constitution, the responsibility of undertakings in respect of post-war reconstruction and development being that of the Provinces, this additional source would come handy.

Per contra, it has been argued that the justification of any measure in affording the necessary funds for social service expenditure would depend on not only in the reduction of excessive and inequitable burden of taxation but also on economising expenditure and diversion of savings for the improvement of the lot of the poor. But if the people of this country are already over-taxed, in the light of the average per-capita income of the country, the opposition argued, it would not be safe to launch on a different tax programme, which would undermine the industrial activity in the country as a whole.

The question of tax-burden should be understood relatively, and the absolute taxable capacity of a country will depend on the industrial production, and on a number of factors. If, as the authors of the Bill profess, the proceeds are to be utilised in furthering the industrial programme, little opposition can be offered. The necessity for large funds for the provinces is patent, and so also the need for a greater expenditure on social services. The first objective of the Bill therefore is very sound.

The second objective which the Bill embodies is that despite the increased taxation that was levied during the war-time, several persons have become fabulously rich, and that due to these private fortunes the inequality has aggravated. Therefore the Finance Minster is of the opinion that if the estate duty is levied, it would be a step

in the process of reducing the widest disparities. This will ultimately bring about an equitable distribution of national income.

The protagonists of estate duty argue that the inequality which exists today is due to the fact that the rich have exploited unscrupulously the poor. If the estate duty is levied and collected from the rich at the time of their death, without allowing the whole property to be inherited, inequality to a great extent will be reduced.

Mr. Barna in an interesting article entitled "Social Significance of Death Duties" stated thus: "From the figures it can be estimated that in 1937 less than 1% of the population possessed about 40% of all capital in personal ownership—a proportion which shows a high degree of inequality in the distribution of capital, though not necessarily higher than in other countries. These persons paid 85% of all estate duties...." Later on discussing about the social importance of death duties, he said that "they tend to bring about a greater equality in the distribution of property through gradual change. High rates of duty have not been in operation long enough yet to have definite results. But it is quite clear that an average rich family cannot pay income tax and surtax at present rates, as well as death duties in each generation out of income, they must sell some of their property to the less rich."

The above-mentioned view is in perfect accord with the so-called "socialistic" or "diffusion of wealth" theory which postulates that it is the function of government to use the power of taxation as an engine of social reparation in checking the growth of large fortunes and in bringing about a more equal distribution of wealth. According to John Stuart Mill, who developed his scheme out of Jeremy Bentham's reasoning, that no person should be permitted to acquire by inheritance more than the amount of a moderate independence. In cases of intestacy the whole property should escheat to the state. It shall be incumbent upon the state, however, to make a just and reasonable provision for descendants, that is, such a

provision as the parent or ancestor ought to have made, their circumstances, capacities and mode of bringing up being considered. An American authority writing about the way in which England had led the way in bringing about a measure of this type wrote: "The English are not much given to abstract reasoning in politics, but in the practical working out of political ideals, England has usually led the way. In finance she has taken a similar lead. She was the first important nation to restrict the scope of taxes on consumption and to introduce the income tax, and during the 'nineties, while the scientists the world over were debating the problem of lessening the burdens on the lower and middle classes she boldly took steps which in many other countries would, to say the least, have been deemed premature. The three great reforms accomplished in England in 1894 were the extension of the inheritance tax, the introduction of the progressive principle and the increase of the minimum subsistence".

In Mr. Layton's memorandum of the Indian Statutory Commission's Report, as early as in 1930, it was clearly emphasised that "though the population of India consists in the main of extremely poor people, it is at the same time a country in which there are large accumulations of wealth on which the burden of government rests very lightly. In spite of the widespread poverty in India, I see no reason to doubt that the public revenues of India can be substantially increased without taxation becoming intolerable, provided that its incidence is adjusted to the capacity of tax-payers to pay and that heavy additional burdens are not put upon primary necessities". In saying so he was surely thinking of death duties. If there is any form of taxation to curb inequality and disparity, it is definitely estate duty, and this is also theoretically justified on grounds of ability to pay, certainty of the payment and convenience in the matter of collection. The duty will be most suitable to those tax-dodgers who have been hoarding the precious metals, and will fall on the inherited property which is most likely to be extravagently spent.

Some Chambers of Commerce raised objections against the Bill on the ground that the estate duty will not satisfactorily remove inequality, and the disparity of income and property. It is arguable that when India is industrially and socially in early stages, it is not advisable to impose a tax of this nature to deprive the industrialists of their wealth, which could otherwise have been utilised in industrial and developmental channels. By attempting to squeeze disparity between the capitalists and the other classes, the Bill would ultimately lessen industrial and agricultural production.

Little do these Chambers realise that when once the estate duty is collected from the inheriting beneficiary, the proceeds are just transferred from the rich capitalists to the State, which eventually comes to the same thing as providing more revenue for expenditure on "social service" and industrial programmes. Thus by depriving the inheritors of the riches to which they laid claim to on their birth equality was attempted, and by a transfer of expenditure from the individuals to the State, the national income also has been increased.

Therefore Sir Josiah Stamp has shrewdly stated: "Although some have attributed the growth of Death Duty taxation to the spread of democratic ideas, it is at least arguable that this apparent connection may not be due to a conscious democratic mastery of the political theory of inheritance, so much as to the force of example in the search for new sources of revenue to meet an increasing growth of expenditure which depends not on the form of government so much as on the growing economic complexity of the modern State. Or, at any rate, we may say that the need of money has acted as an incentive in the search for an appropriate political philosophy".

Hindu Code and Estate Duty Bill

The Preliminary Report of the Select Committee on the Estate Duty Bill, 1948 embodied the statement that "the application of the Estate Duty Act would be well nigh impossible so long as the joint family under the Mitakshara system continued to be recognised by law as

a unit for purposes of taxation. The levy of any duty on the death of a member of a Hindu co-parcenary is foreign to the fundamental principle of co-parcenary under the Mitakshara law. No individual member of such family can predicate that he has a definite share in the property. His interest is a fluctuating interest capable of being enlarged on deaths in the family or liable to be diminished by births. The provisions of the Hindu Code regarding succession or the structure of a joint family would have a considerable bearing as to how the duty should be levied on the death of a member of such family, and it was, therefore, urged that the consideration of the Bill should await the passing of the Hindu Code."

Parts V, VI and VII of the Hindu Code deal with the reforms that are to be brought about in the "Joint family Property" system, "Woman's Property" rights, and the law of "Succession". These parts introduce changes of a very far-reaching character in the Family Law and the law regarding Ownership of Property. Almost all the provinces and states are governed to-day by the Mitakshara system, and it is only the West Bengal and certain tribal and agricultural areas in the East Punjab that follow the Dayabhaga.

The Hindu Code seeks to alter the present rules of intestate and testamentary succession, and adopt in its stead the Dayabhaga. The argument underlying the alteration is that the joint family is fast breaking up due to changed economic and other circumstances, and that a comprehensive law of succession like the Dayabhaga which precludes the possibility to share the estate of an ancestor during his lifetime would be most salutary. Therefore no court will recognise after the Hindu Code Bill will be passed, any right to or interest in any joint family based on the rule of survivorship and on the date of the enactment of the Bill (Hindu Code Bill) all those persons holding any joint-family property would be deemed to have effected a division of the same, and thereafter the property would be conceived as one of that of "tenants-in-common" thereby giving exclusive right or rights to the

individual members of the family in respect of their own property.

The provision for simultaneous heirs embodied in clause 4, Class I, clause (i) that widow, son, daughter, son of a predeceased son are entitled to succeed simultaneously each getting one share while the daughter has to get half a share. After the Hindu Code Bill becomes law the property of the male Hindu dying intestate will naturally evolve formerly on the preferential heirs of the order of widow, daughter, son of a predeceased son, widow of a predeceased son, etc. The property would be so shared that the widow will obtain as much as the share of each son and the daughter half as much as of the son.

Then there is the provision in the Hindu Code Bill that any property acquired by a Hindu woman after the Bill becomes law shall be her "absolute property." The previous conception of "limited property" has been abandoned. This had occurred as a result of the Rau Committee's recommendations. This "simultaneous property" principle was never adverted to till 1937 when for the first time the Deshmukh Bill was introduced with the main object of giving relief to women coming into the family by marriage. The economic aspect of this revolutionary change had been put before the Rau Committee as follows: In addition, there is an economic factor in the problem. It has been pointed out by several correspondents that in a poor country like India the distribution of a man's estate amongst the widow, the son, the son's widow, the daughter and possibly the mother as well, will inevitably result in the dissipation of such little property as there may be in the country. Whatever may be the ultimate solution of this problem, we feel that it could be investigated adequately only in an inquiry embracing the whole law of succession".

It should be maintained that the Hindu Code Bill goes further than the "Deshmukh" Act. Under the latter, the son, widow and daughter-in-law inherited the property according to the law of survivorship and the widow and the daughter-in-law were entitled to a

"limited estate," which is otherwise known as the "widows' estate." But according to the Hindu Code Bill the son, grandson, great grandson, the widow and the daughter-in-law and parents fall into the category of simultaneous heirs without the right of survivorship and it is proposed that the widow and the daughter should be given the right to absolute estate. According to the law at present, anybody who wishes to be outside the joint family unit should compulsorily seek partition. But according to the proposed law, succession though simultaneous or rather spontaneous would be separate and every person in the family holds an independent share. Thus the widow and daughter obtain absolute estate or rights to property as opposed to the present conception of limited estates or rights to property. The effects of such a change are: Firstly, it leads to an excessive fragmentation of land. Though for the time being this Bill does not apply to agricultural land, sooner or later it will do so. The Estate Duty Bill that is at present under discussion is thus greatly affected by the provisions of the Hindu Code Bill.

Secondly, the oneness in the joint family unit is rudely shaken. Where joint family system exists the economic stability can be the order of the day, and where it is broken up economic survival would be very difficult. Capacity to borrow would also naturally be undermined, with the result that on the one hand the purchasing power would be affected, and on the other the lending power of the creditor. It has been maintained that "Joint family system is still found prevalent in all parts of India and particularly in villages as it is an economic expedient to enable a large number of persons belonging to the same family to live together under one roof and maintain themselves out of the joint income earned by them. The disruption of the joint family system would add to the existing poverty of the country."

The difficulty that the Dayabhaga and Mitakshara differ in fundamentals is already noted. That the Malabar *Tarawad* system under which the individual

members cannot either lay claim to partition of the *Tarawad* property or any right of testation and that it would be more or less impossible to tax the undivided interest in the *Tarawad* property need not deter us from passing the Estate Duty Bill. The Hindu Code Bill may bring about a complete overhaul in the social structure and once that is done, there will be a universal and comprehensive social law, on which succession can be based and the estate duty collected with ease and convenience.

Important Sections of Estate Duty Bill

The Estate Duty Bill which was introduced in the Constituent Assembly (Legislative) by Sir R. K. Shanmukham Chetty, the then Finance Minister, contains seventy sections.

Section 6:

This deals with the interests ceasing on death, lays bare that property in which the deceased or any other person had any interest at the time of his death shall be taken for granted as having been passed to the extent to which a benefit accrues or arises by the cessor of such interest. This interest might include any co-parcenary interest of the joint family property. The co-parcenary interest in the joint Hindu family goverened by the Mitakshara school towards this interest is one which passes on the death of the co-parcenary at the time of his decease. In fact, the correct legal position is that the co-parcenary interest remains joint till it is divided and should be determined as and when the division takes place. There would be no question of separate interest unless the joint family system has been disturbed. The Hindu joint family remains a composite entity and remains so for all practical purposes for any taxation. The income-tax, in fact, goes a step further and under section 25 (a) of the Act an order has to be passed before the family is going to be divided. Even, though the family is divided but if such an order has not been passed, the family should be treated from the point of view of the

levy of income-tax as undivided. Thus, a fictitious position, as it were, subsists despite the fact that the Hindu family remains joint until the division is effected. The Estate Duty Bill brings about another interest which is not permissible under Hindu Law. That is why it is often said that this Bill would affect the co-parcenary property when enacted. In fact, according to the Hindu Law, co-parcenary should be kept aloof from the Bill. It is often, therefore, suggested that section 6 should undergo a vital change and, it should be stated that the Bill does not even in the least have any repercussions on the co-parcenary property. Due to the high rate of mortality in the country and owing to the size of the joint Hindu family, the collection of the estate duty might even be restricted to the occasion of the death of a co-parcenary of the old generation. Infant mortality, more often than the authors of the Bill conceived, reduces the joint family property to unforeseen minima. Administrative difficulties would also creep in with the inclusion of the co-parcenary interest, as the interest varies with the birth and death of the members of the joint Hindu family, with the result that the estate would be chargeable to estate duty several times in the life of any one member of the joint Hindu family.

The select Committee on the Estate Duty Bill which recently met, in their interim report, mentioned that this section would not be able to afford adequate justice in the light of the complex problems that might arise in the matter of the Hindu Law of Succession or the modifications that might be brought about with the enactment of the Hindu Code. Later on, after the enactment of the Hindu code it is said that the section 6 can be so widened, so that the determination of the deceased's interest and the tax payable thereafter may be treated for a short length of time, the charge being modulated after the lapse of that period. The charge of tax might even lead to division of the Hindu joint family property, or the joint family will bear the charge from its estate so long as the family remains undivided.

Sections 7, 8, and 9:

In these sections it has been shown how estate duty should be levied on gifts. All the gifts given by the deceased in contemplation of death would be naturally deemed to have been passed on to the donee. The property taken under disposition made by the deceased purporting as a minimum gift *inter vivos* made three years or more before his death would also be deemed to have been passed on to the donee.

Hindu Law recognises gifts *causa mortis,* that is, those given in contemplation of death and gifts *inter vivos* in respect of the property that the deceased acquired, can be legally maintained. But the Estate Duty Bill does not recognise the property given out as gifts in contemplation of death. The right of *donatio mortis causa* is being taken away from the Hindu family. With regard to gifts *inter vivos* that is, gifts made by the deceased in respect of property acquired, the law will be that all those gifts given within three years before the death, would be deemed to have passed to the donee on his death. The Indian Taxation Enquiry Committee in its report clearly stated: "It is desirable, in so far as it is practicable, to include within the scope of the duty gifts made within a year of death, which should be treated for purposes of this duty as part of the assets of the estate". * This goes against the tenets of Muslim Law relating to *hyba* made in *Marz-ul-Maut.* The meaning of this phrase "in contemplation of death" is not the same as that expressed by Lord Robertson "under the pressure of the sense of the imminence of death". With respect to gift made by a Muslim on his death bed, according to his Law, one-third of the estate can be transferred after the payment of the funeral expenses and debts, if any. The right to sanction gifts to one-third of the estate is recognised according to the Muslim Law, and the sections relating to the gifts in the Estate Duty Bill come into conflict directly with it.

The period of three years or more before the death of the deceased is too long, and it is suggested that it

* Taxation Enquiry Committee, p. 275, (Section 372).

should be reduced to one year, since the estate duty has not yet been introduced in this country. There should not be any limitation on gifts for charitable purposes. Similar provisions are embodied in Acts of the United Kingdom and Australia, and some other countries.

Sections 16, 17 and 18:

The provisions relating to transfers and companies can be elaborated under the following heads:

Firstly, property transferred to a controlled company. (Section 16)

Secondly, Companies' duty in this respect (Sec. 17)

Thirdly, collection and incidence of duty (Sec. 18).

Since the Central Board of Revenue will draft the rules regarding controlled companies and matters connected with it and the legislature will have no hand in the matter, everything is left to executive discretion. While the English Act is quite definite, the Indian Estate Duty Bill does not cover the definitions of the controlled companies and transfers.

According to the Bill, the assets of a company are assessable to duty, firstly, when the deceased had made a transfer of his self-acquired property to controlled company. This property should neither be the one comprising limited interest which ceases on his death, nor could it be held in a fiduciary capacity; secondly, the benefits derived by the deceased from the company must have accrued to him three years before his death. The correct amount of the benefits accruing to the deceased from the company in the three last accounting years should be compared with the aggregate amount of the net income of the company during the same period and the proportion between them should be ascertained. But if due to unforeseen circumstances, the Company had sustained a grievous loss during those years, according to the Bill, relief would naturally be provided in as much as the amount of that loss is deductible in ascertaining the said aggregate income of the company. If supposing the Company has come into existence only in the last of the three years, then it would be

reckoned as referring to the last of the two or three years as the case may be.

It would be interesting to note as to what the non-taxable assets of the Company would comprise of.

(i) Those assets which a company might part with either by sale or by other means for full consideration in money or in money's worth, in its own interest and for its own benefits.

(ii) Taxation or any other liability may warrant the distribution of some of the assets of the company, in which case such assets would be exempt from any levy of death duty.

(iii) The contingent liabilities by way of fine or a liability in tort which may force on a company a compulsory disposition of its assets would be exempt from the duty. Finally the distribution or disposition of assets of a company may take place in the shape of payments from which income-tax was deductible or on which income-tax might be levied, in which case such assets are also not chargeable to estate duty.

What then are the taxable assets of a company? The taxable assets of a company consist of those assets "which a company parts with or distributes either towards the satisfaction of rights attached to shares or towards redeeming of the debentures of the company; but it is absolutely essential that those assets must have been disposed of or distributed at any time between the beginning of the first of the accounting years and the death of the deceased."

Section 13 :

Section 13 deals with the estate duty devolving on life and other Insurance Policies. Life-Insurance is still in its infancy in this country and any tax on a policy taken for the benefit of the donee, nominee or assignee would retard its growth and as such, the imposition of tax on life insurance does not seem to be fair. The argument for exempting estate duty on life insurance is that in most cases insurance will be effected with a view to affording the minimum amount of money required to

keep the family above the barest requirements of life and maintenance. It would not be in the interests of the family as a whole that the minimum requirements should be taken away by a tax on the insured sums. The Indian Life Assurance Offices' Association, Bombay, in their opinion on the Estate Duty Bill drew the attention of the Government to recognise "the essential difference between the estate represented by investments and that represented by proceeds of Life Assurance and Annuities. In the former, the income is enjoyed by the investor during his life-time while the latter is created mostly due to a spirit of self-abnegation and love for near and dear ones". The Association therefore felt that "if an individual is mulcted of a part of the property accumulated under the dictates of such motives by imposition of an estate duty without granting exemption upto a reasonable amount, the result would be retardation in the insuring habit of moderately well-placed families in India". Citing instances of exemption, they said that "the Federal Estate Tax Law in America provides an exemption to policies of life assurance to the extent of $40,000 payable to individual beneficiaries without any stipulation as regards the payment of premiums as contemplated in the present bill. . . . The principles of allowing exemption to life assurance premiums to a certain reasonable limit from assessment to income tax on ground of 'mitigation of taxation of savings' has already been recognised by the Government of India under Section 15 of the Indian Income Tax Act, under which annual premiums of life assurance and annuities upto the extent of Rs. 6,000 are exempted from income tax. The Association submits that the principle already recognised in the Indian Income Tax Act, should also be applied to estate duties and that an exemption should be granted to the proceeds of life assurance policies and annuities from the levy of estate duties, at least to the extent of policies of life assurance for the amount of Rs. 1,00,000 or in the alternative to an amount of life assurance policies and annuities represented by an annual premium of Rs. 6,000."

Here we may recall the view of Mr. Beaumont Pease : "In partnerships and in the case of large estates, death duties are largely provided for by life insurance out of income. It has always seemed to me that it is a great hardship that such provision made out of income should itself be subject to death duties and should in many cases actually increase the rate of such duties payable by the estate. I think it would greatly encourage the provision for such duties by insurance which economically is a very sound thing to do if the provision itself were exempted subject to proper limitations and safeguards." *

A similar provision in the Australian Estate Duty Assessment Act 1914, was included by an amendment to the same in the year 1942. It runs as follows:—

"Property—

8. (4) (f) being money payable to, or to any person in trust for, the widow, widower, children, grand-children, parents, brothers, sisters, nephews or nieces of the deceased under a policy of assurance on the life of the deceased where the whole of the premiums has been paid by or on behalf of the deceased, or, where part only of the premiums has been paid by or on behalf of the deceased, such portion of any money so payable as bears to the whole of that money the same proportion as the part of the premiums paid by or on behalf of the deceased bears to the total premiums paid" ;

shall for the purposes of this Act be deemed to be part of the estate of the person so deceased."

Section 19:

Section 19 deals with the foreign property which can be excluded from the imposition of the estate duty. Under this section many foreigners can escape the duty. Under Section 3 (c) it is laid down that the domicile of

* Committee on National Debt and Taxation, **Minutes of Evidence, Vol. 1, p. 319.**

a person shall be determined as if the provisions of the Indian Succession Act, 1925 (XXXIX of 1925) on the subject applied to him. It can be summarised as follows:

"(i) succession to the immovable property in British India of a person deceased shall be regulated by the Law of British India wherever such person may have had his domicile at the time of his death.

(ii) succession to the movable property of a person deceased is regulated by the law of the country in which such person had his domicile at the time of his death."

That means that movable property located outside British India cannot come within the compass of the duty unless the deceased at the time of his decease is domiciled in British India. Domicile according to the Act means that the deceased should have had taken up a fixed habitation with the fixed intention of residing there during his life. Thus much scope is given for many foreigners who come to this country on profession or business to escape taxation legally, though they earn money here. There is no reason why they should be exempt from taxation, which falls severely on those who are domiciled here.

The Select Committee in their Preliminary Report on the Estate Duty Bill apprehended that "under clause 19 of the Bill immovable property so situate outside the provinces of India is exempt and movable property so situate is also exempt in certain circumstances. This would mean the flight of capital to Indian states for invesment in immovable and movable properties, unless the states also introduce similar legislation and bring their level of taxation to that prevailing in the provinces of India. The question of integration of fiscal policy of the states with that of the Government of India has been taken up, but it would be some time before the relationship of the States with the Centre and their fiscal obligations and rights are determined and stabilised." This reason is

not a conclusive one, and till efforts are made in bringing the states on a par with the provinces in matters of taxation and taxation policies. Taxes enumerated in the Central list under the Government of India Act, 1935 (as adapted in August 1947) should be taken over by Central Government from the states, and the states should be so compensated on the basis of the yield of the taxes, like income-tax, excise, customs, etc. There is no difficulty at present in the matter of the states as almost all states have joined the Indian Union, and have been integrated into one or another Union. Till the relationship of the states with the Centre is determined, finally, some workable solution can be adopted.

Section 29:

This tries to provide some allowance by reducing the percentage whenever a second death occurs within five years, of the first. The striking factor is that five years is too short a period, particularly because of the high rate of mortality in India. Even in Western countries where man's life is longer, the period allowed from the first death for matters of the levy of estate duty to the second death is also longer. In the United States no levy is made on the second succession if it occurs within five years of the first death. In Japan only 50% of the basic rate has to be paid if the third death occurs within two years of the second death, with a a full exemption from the charge if the second succession occurs within five years of the first. In Chile, law prohibits any levy on second succession within a period of ten years. Looking at these specific instances, greater relief should be afforded in quick and quicker successions, particularly because of the high rate of mortality prevailing in this country. Otherwise, there would be such a widespread discontent that the public may be tempted to try all possible means of avoiding and evading the tax.

Section 30:

According to this section the Central Government is statutorily authorised to notify exemptions or reductions in favour of any class of property. This will enable the

government to decide whether exemption can be given to any investments in preference to some others. Under the present income-tax law, the insurance habit is favoured and exemptions are given for insurance and provident fund contributions. "The opportunities which Section 30 affords for encouraging capital formation of certain kinds should be used as early as possible to direct savings into nationally useful channels."

Section 31:

This section provides for the aggregation of the property and the levy of a graduated rate on the principal value thereof. This makes the position quite clear that the levy is not on the individual shares of property inherited by say all the sons in a joint family of the Hindu society. In fact, difficulty arises in a joint family as to how the levy should be imposed, unless it is by this method. Succession and legacy duties that are being imposed in countries like the United Kingdom are not feasible. As the Advocate-General of the Central Provinces stated: "The basic rate may be kept high with provision for rebates upto a pre-determined maximum on that part of the estate which passes to the widow, children and grand-children of the descendant. In the case of a joint Hindu family governed by Mitakshara the descendant's brother and his widow, children and grand-children and the widows of the son and the grand-son of the descendant and his brother may be treated likewise for the purpose of rebates."

But with the enactment of the Hindu Code, conditions would naturally undergo a vital change. The scope for succession and legacy duties will be probably great. It does not mean that till the passing of the Hindu Code, the estate duty bill could be withheld. Equal property rights for women will certainly bring out the necessity for legacy and succession taxation. Otherwise, there will be the widest scope for avoidance and evasion of estate duties, with the breaking up of the joint family.

Section 32:

The rates of the duty are not yet specified in the present Bill, but it is stated that "no such duty shall be levied upon estates whose principal value does not exceed Rs. one lakh;" and "that by way of marginal adjustment, the amount of estate duty payable on an estate at the rate applicable thereto under the scale of rates of duty shall, where necessary, be reduced so as not to exceed the highest amount of duty which would be payable at the next lower rate, with the addition of the amount by which the value of the estate exceeds the value on which the highest amount of duty would be so payable at the lower rate."

The proposal regarding the rate of the duty as given out by the Taxation Enquiry Committee is as follows:—

	Rs.	Per cent.
	5,000	Nil
Next	5,000	½
,,	10,000	1
,,	30,000	1½
,,	50,000	2
,,	1,00,000	2½
,,	3,00,000	3
,,	5,00,000	4
,,	10,00,000	5
,,	20,00,000	6

The Report contains the following passage: "It is therefore recommended that, alike for the purpose of introducing a general inheritance tax in India on the lines of least resistance, and for that of removing the inequalities in the incidence of the existing probate duties, and as a necessary measure of law reform, an attempt should be made to introduce a system of representation on the lines of those in force in the United Kingdom, in other words, to extend the existing law of probate to all communities. To ensure the success of the scheme in the initial stages, the limit of exemption should be placed not

lower than Rs. 5,000, and on sums exceeding that figure, the duty payable should not be high."

Thus the Taxation Committee suggested that no duty should be levied on Rs. 5,000. The present Bill provides that the limit of exemption should be put at Rs. 1,00,000. The difference between the limit proposed by the Taxation Enquiry Committee and that embodied in the present section is too much. When the Taxation Enquiry Committee made its recommendations, the boom period after the first World War had run its full race and slump was facing them. And after the recommendations came the Second World War when enormous private fortunes were made; and war-time taxation could not hit at all the abnormal incomes and profits, a good proportion of which escaped taxation.

The Committee of Economists appointed by the Government of India in September 1948 to give their recommendations for effectively dealing with the menace of inflation stated that "immediate and determined action is called for to prevent further deterioration of the situation, since there is a real danger of run-away inflation unless effective action is taken without further delay," and so one of their main taxation proposals was that "steeply graduated death duties should be introduced without delay." The Congress Party Sub-Committee came to the conclusion that "death duties should be imposed as early as possible." It is true that death duties will not be immediately effective, because introduction itself will take time. As death duties fall on the death of persons, they might not be so effective during a short period. But in the long period the duties are bound to be productive. The exemption limit prescribed under this section is too high. Considering the economic and business conditions it has been suggested that the level of exemption should be brought down to Rs. 50,000, above which the duty may be graduated to Rs. 20,00,000 and over on a steeply rising scale which may range from 1% to 50%. On the other hand, some say even Rs. 1,00,000 is too meagre and that the exemption limit

should be raised to Rs. 5,00,000. In the U. K., the minimum taxable amount had been fixed at £100; from April 10, 1946, however it was raised to £2,000. Experience of most of the countries has been in favour of fixing the exemption limit in the beginning at a low level, so that it could be raised as and when necessary. The lower the exemption the more effective it will be to curb inflation.

Section 33:

This section mentions that the principal value of any property shall be estimated to be the price which it would fetch if sold in the open market at the time of the deceased's death. The United States Federal Estates Tax Rules permit the executor to valuate all property either at the date of the death of the deceased or an year after. It would be advisable to incorporate a provision of this character, so as to allow deduction for depreciation when the price of shares fall after the death of the deceased.

Section 40:

This section provides for allowances in certain cases in the determination of the value of the estate. According to the Hindu Law, three kinds of debts are allowed: (i) debts incurred for the purpose of the family; (ii) debts incurred for one's own purpose but which are neither illegal nor immoral, and (iii) debts incurred for illegal or immoral purposes. The first two debts have to be paid by the successors of the deceased, out of their shares from the joint family property.

The section also provides for *bona fide* debts incurred for one's own use to be deductible in the determination of the value of the estate. There might also be some debts incurred in the business routine as guarantor on behalf any contracting party. These do not fall within the scope of this section.

Section 54:

This section gives the Board the authority to revalue the property in respect of which estate duty is to be

paid. The High Court should be empowered to appoint valuers, and the valuer's decision should be treated as final.

Distribution of Proceeds of the Duty

The proceeds of the Estate Duty are mainly intended according to the Bill for the benefit of the provinces. "On strictly logical grounds," says the American Committee, "a very strong case could be made for separation of sources as a co-ordination device in the death tax field. The State tax is plagued by the fact that estates are highly concentrated in a relatively few States, though the wealth represented may have been accumulated over a much wider area. On the other hand, the States, with one exception, have a proprietary interest in this field and any proposal for surrender would rouse intense antagonism. Moreover, any method of getting the States out of the field, short of a constitutional amendment, would involve a distribution of revenues not very difficult from the present." *

The Expert Committee on the Financial Provisions of Union Constitution, appointed by the President of the Constituent Assembly of India, in their report observed thus: "Estate and Succession Taxes—these taxes have not so far been levied. One of the hurdles to be crossed before they can be levied is the determination of the manner of distribution of the net proceeds among Provinces. Until the taxes are actually levied and collected for some time, no data about their incidence will be available. Hence, the levy will have to start with some *a priori* basis of apportionment among Provinces. We accordingly recommend that until the Finance Commission is in a position to evolve a better method on the basis of data available to it, the net proceeds should be distributed among the Provinces as follows:—

* Senate Document No. 69, 78th Congress—Report of Committee on Intergovernmental Fiscal Relations, Major Conclusions and Recommendations, Vol. i, chap. iv.

The net proceeds attributable to real property—
On the basis of the location of the property.

Of the balance—

75% on the basis of the residence of the deceased.

25% of the basis of the population of the Province."

There were of the opinion that if the Centre had to forego a substantial amount of taxes on income and also a portion of the Central excise, it would be most appropriate that it should claim a slice of the estate and succession duties. This would for certain, create direct interest in the imposition and collection of the duties. The Committee recommended a 40% share to the Centre. They have also suggested amendments to the Constitution as follows: "196. *Certain Succession Duties*: (1) Duties in respect of succession to property other than agricultural land and estate duty in respect of property other than agricultural land shall be levied and collected by the Federation, but 60% or any higher figure as may be prescribed of the net proceeds in any financial year of any such duty, except in so far as those proceeds attributable to Chief Commissioners' Provinces, shall not form part of the revenues of the Federation, but shall be assigned to the units within which that duty is leviable in that year, and shall be distributed among the units in accordance with such principles of distribution as may be prescribed.

(2) If any dispute arises as to the distribution of the net proceeds of any such duty among the units, it shall be referred for decision to such authority as may be appointed in this behalf by the President and the decision of such authority shall be final."

In conclusion, it is right that an understanding should be reached between the Central Government and the Provincial and States Governments so that a certain proportion of the proceeds of the estate duty will accrue to the Centre, as in the case of income tax, Central excise, and other taxes. That would give the Central Government a direct incentive to collect death duties.

APPENDIX 1

A BILL TO PROVIDE FOR THE LEVY AND COLLECTION OF AN ESTATE DUTY IN THE PROVINCES OF INDIA

Whereas it is expedient to provide for levy and collection of an estate duty in the provinces of India;

It is hereby enacted as follows:—

PART I.—INTRODUCTORY

1. Short title, extent and commencement.—(1) This Act may be called the Estate Duty Act, 1946.

(2) It extends to all the provinces of India.

(3) It shall come into force on such date as the Central Government may, by notification in the official Gazette, appoint in this behalf.

2. Definitions.—In this Act, unless there is anything repugnant in the subject or context,—

(1) "affidavit of valuation" means the affidavit of valuation made under section 19 I of the Court-fees Act, 1870 (VII of 1870), in connection with an application for the grant of representation;

(2) "the Board" means the Central Board of Revenue constituted under the Central Board of Revenue Act, 1924 (IV of 1924), and, if in respect of any matter the Central Government has empowered any officer or authority to discharge the functions of the Board, includes that officer or authority in respect of that matter.

(3) "company" includes any body corporate wheresoever incorporated;

(4) "controlled company" means a company which is deemed to be controlled by virtue of the rules prescribed under sub-section (4) of section 16;

(5) "deceased person" and "the deceased" mean a person dying after the commencement of this Act;

(6) "estate duty" means estate duty under this Act;

(7) "executor" means the executor or administrator of a deceased person and includes, as regards any obligation under this Act, any person who takes possession of, or intermeddles with, the estate of a deceased person or any part thereof;

(8) "general power" includes every power or authority enabling the donee or other holder thereof to appoint or

dispose of property as he thinks fit, whether exercisable by instrument "inter vivos" or by will or both, but exclusive of any power exercisable in a fiduciary capacity under a disposition not made by himself or exercisable as mortgagee;

(9) "incumbrances" includes mortgages and terminable charges;

(10 "interest in expectancy" includes an estate in remainder or reversion and every other future interest whether vested or contingent, but does not include reversions expectant upon the determination of leases;

(11) "power to appoint property" means power to determine the disposition of property of which the person invested with the power is not the owner;

(12) "prescribed" means prescribed by rules made under this Act;

(13) "property" includes any interest in property movable or immovable, and the proceeds of sale thereof and any money or investment for the time being representing the proceeds of sale;

Explanation.—(1) The creation by a person or with his consent of a debt or other right enforceable against him personally or against property which he was or might become competent to dispose of, or to charge or burden for his own benefit, shall be deemed to have been a disposition made by that person, and in relation to such a disposition the expression "property" shall include the debt or right created.

(2) The extinguishment at the expense of the deceased of a debt or other right shall be deemed to have been a disposition made by the deceased in favour of the person for whose benefit the debt or right was extinguished, and in relation to such a disposition the expression "property" shall include the benefit conferred by the extinguishment of the debt or right.

(14) "property passing on the death" includes property passing either immediately on the death or after any interval, either certainly or contingently, and either originally or by way of substitutive limitation, and "on the death" includes "at a period ascertainable only by reference to the death";

(15) "representation" means probate of a will or letters of administration;

(16) "settled property" means property which stands limited to, or in trust for, any persons, natural or juridical by way of succession, whether the settlement took effect before or after the commencement of this Act; and "settlement" means any disposition, including a dedication or endowment, whereby property is settled.

3. **Interpretation.**—(1) For the purposes of this Act—

(a) a person shall be deemed competent to dispose of property if he has such an estate or interest therein or such general power as would, if he were "sui juris" enable him to dispose of the property.

(b) a person shall be deemed to dispose of property to which he has acquired title even if he has acquired title to it in one form and disposes of it in another;

(c) a disposition taking effect out of the interest of the deceased shall be deemed to have been made by him, whether the concurrence of any other person was or was not required;

(d) money which a person has a general power to charge on the property of another person shall be deemed to be an interest in that property of which the former has power to dispose;

(e) the domicile of a person shall be determined as if the provisions of the Indian Succession Act, 1925 (XXXIX of 1925), on the subject applied to him.

(2) In Parts II and III of this Act, any reference to any interest disposed of, policy of insurance effected, annuity or other interest purchased or provided or to any gift, settlement, disposition or transfer of property made, shall be construed as including any such interest, policy, annuity, gift, settlement or disposition, as the case may be, whether it was disposed of, effected, purchased or provided, or made before or after the commencement of this Act.

PART II.—IMPOSITION OF ESTATE DUTY

Extent of Charge

4. **Levy of estate duty.**—In the case of ever person dying after the commencement of this Act, there shall, save as hereinafter expressly provided, be levied and paid upon the principal value ascertained as hereinafter provided, of all property, settled or not settled, not being agricultural land, which passes on the death of such person, a duty called "esate duty" at the graduated rates hereinafter mentioned.

Property Which is Deemed to Pass

5. **Property within disposing capacity.**—Property which the deceased was at the time of his death competent to dispose of shall be deemed to pass on his death.

6. **Interests ceasing on death.**—Property in which the deceased or any other person had an interest ceasing on the deceased's death shall be deemed to pass on his death to the extent to which a benefit accrues or arises by the cesser of

such interest, including, in particular, a copaŕcenary interest in the joint family property of a Hindu family governed by the Mitakshara school of law, but exclusive of property in which the deceased or other person had an interest only as holder of an office or recipient of the benefits of a charity, or as a corporation sole.

7. **Gifts mortis causa.**—Property taken as a gift in contemplation of death shall be deemed to pass on the donor's death.

8. **Gifts within a certain period before death.**—Property taken under a disposition made by the deceased purporting to operate as an immediate gift **inter vivos** whether by way of transfer, delivery, declaration of trust, settlement upon persons in succession, or otherwise, which shall not have been **bona fide made three years or more** before the death of the deceased shall be deemed to pass on the death:

Provided that in the case of gifts made for public or charitable purposes the period shall be twelve months and not three years.

9. **Gifts whenever made where donor not entirely excluded.**—Property taken under any gift, whenever made, shall be deemed to pass on the donor's death, if **bona fide** possession and enjoyment of it was not immediately assumed by the donee and thenceforward retained to the entire exclusion of the donor or of any benefit to him by contract or otherwise:

Provided that the property shall not be deemed to pass by reason only that it was not, as from the date of the gift, exclusively retained as aforesaid, if, by means of the surrender of the reserved benefit or otherwise, it is subsequently enjoyed to the entire exclusion of the donor or of any benefit to him for at least three years before the death.

10. **Limited interests disposed of within a certain period before death.**—(1) Subject to the provisions of this section, where an interest limited to cease on a death has been disposed of or has determined, whether by surrender, assurance, divesting, forfeiture or in any other manner (except by the expiration of a fixed period at the expiration of which the interest was limited to cease), whether wholly or partly, and whether for value or not, after becoming an interest in possession,—

(a) if apart from the disposition or determination the property in which the interest subsisted would have passed on the death under section 4, that property shall be deemed by virtue of this section to be included as

to the whole thereof in the property passing on the death; or

(b) if apart from the disposition or determination the property in which the interest subsisted would have been deemed by virtue of section 6 to be included to a particular extent in the property passing on the death, the property in which the interest subsisted shall be deemed by virtue of this section to be included to that extent in the property passing on the death.

(2) Where the relevant disposition or determination was "bona fide" effected or suffered not less than three years before the death (or, if it was effected or suffered for public or charitable purposes, not less than one year before the death), the preceding sub-section shall not have effect—

(a) if "bona fide" possession and enjoyment of the property in which the interest subsisted was assumed immediately thereafter by the person becoming entitled by virtue of or upon the disposition or determination and thenceforward retained to the entire exclusion of the person who had the interest and of any benefit to him by contract or otherwise; or

(b) in the case of a partial determination, if the conditions specified in the preceding paragraph were not satisfied by reason only of the retention or enjoyment by the deceased of possession of some part of the property, or of some benefit, by virtue of the provisions of the instrument under which he had the interest:

Provided that nothing in this sub-section shall be construed as affecting any charge of estate duty arising otherwise than by virtue of the provisions of the preceding sub-section.

(3) In the application of sub-section (1) to a case in which an incumbrance on the property in which the interest in question subsisted has been created by associated operations (as hereinafter defined in section 25) which included a disposition of that interest, references to that property shall be construed as references to that property free from the incumbrance, except in a case in which the incumbrance was created for consideration in money or money's worth which was applied for purposes calculated to maintain or increase the value of that property, and, in that case, shall be construed as references to that property subject to the incumbrance to the extent to which the consideration was so applied.

11. Settlements with reservation.—Property passing under any settlement made by the deceased by deed or

any other instrument not taking effect as a will whereby an interest in such property for life or any other period determinable by reference to death is reserved either expressly or by implication to the settlor or whereby the settlor may have reserved to himself the right by the exercise of any power, to restore to himself or to reclaim the absolute interest in such property shall be deemed to pass on the settlor's death.

Explanation.—A settlor reserving an interest in the settled property for the maintenance of any of his relatives (as defined in section 25) or of himself and any of his relatives shall be deemed to reserve an interest for himself within the meaning of this section.

12. **Joint investments.**—Property which a person, having been absolutely entitled thereto, has caused to be transferred to or vested in himself and any other person jointly, whether by disposition or otherwise, including any purchase or investment effected by the person who was absolutely entitled to the property, either by himself alone, or in concert, or by arrangement, with any other person, so that the beneficial interest in the property, or in some part of it, passes or accrues by survivorship on his death to the other person, shall be deemed to pass on the death.

13. **Policies kept up for a donee.**—Money received under a policy of insurance effected by any person on his life, where the policy is wholly kept up by him for the benefit of a donee, whether nominee or assignee, or a part of such money in proportion to the premiums paid by him, where the policy is partially kept up by him for such benefit, shall be deemed to pass on the death of the assured.

14. **Annuity or other interest purchased or provided by the deceased.**—Any annuity or other interest, including moneys payable under policy of life assurance, purchased or provided by the deceased, either by himself alone or in concert or by arrangement with any other person shall be deemed to pass on his death to the extent of the beneficial interest accruing or raising, by survivorship or otherwise on his death.

Explanation.—The extent of the beneficial interest must be ascertained without regard to any interest in expectancy which the beneficiary may have had therein before the death.

15. **Annuity or other interest purchased or provided out of property derived from the deceased.**—(1) Section 14 shall have effect in relation to any annuity or other interest that was purchased or provided wholly or in part by any person who was at any time entitled to, or amongst whose resources there was at any time included, any property

derived from the deceased, as if that annuity or other interest had been provided by the deceased, or, if it is proved to the satisfaction of the Board that the application of all the property derived from the deceased would have been insufficient to provide the whole of that annuity or other interest, as if a similar annuity or interest of an amount reduced to an extent proportionate to the insufficiency proved had been provided by the deceased:

Provided that for the purpose of determining whether there would have been any such insufficiency as aforesaid, and the extent thereof, there shall be excluded from the property derived from the deceased any part thereof as to which it is proved to the satisfaction of the Board that the disposition of which it, or the property which it represented, was the subject-matter, was not made with reference to, or with a view to enabling or facilitating, the purchase or provision of the annuity or other interest, or the recoupment in any manner of the cost thereof.

(2) In this section the following expressions have the meanings hereby assigned to them respectively, namely:—

(a) "property derived from the deceased" means any property which was the subject-matter of a disposition made by the deceased, either by himself alone or in concert or by arrangement with any other person, otherwise than for full consideration in money or money's worth paid to him for his own use or benefit, or which represented any of the subject-matter of such a disposition, whether directly or indirectly, and whether by virtue of one or more intermediate dispositions and whether any such intermediate disposition was or was not for full or partial consideration;

(b) "disposition" includes any trust, covenant, agreement or arrangement; and

(c) "subject-matter" includes, in relation to any disposition, any annual or periodical payment made or payable under or by virtue of the disposition.

(3) For the purpose of section 31 the deceased shall be deemed to have had an interest in any property included by virtue of this section in the property passing on the death of the deceased.

Special Provisions Relating to Transfers to Companies

16. **Property transferred to a controlled company.**—(1) Where the deceased has made to a controlled company a transfer of any property (other than an interest limited to cease on his death or property which he transferred in

a fiduciary capacity), and any benefits accruing to the deceased from the company accrued to him in the three years ending with his death, the assets of the company shall be deemed for the purposes of estate duty to be included in the property passing on his death to an extent determined in accordance with sub-section (2) of this section.

(2) The extent to which the assets of the company are to be deemed to be included as aforesaid shall be the proportion ascertained by comparing the aggregate amount of the benefits accruing to the deceased from the company in the last three accounting years with the aggregate amount of the net income of the company for the said years.

Provided that—

(a) where, in any of the said accounting years, the company sustained a loss, the amount of that loss shall be deducted in ascertaining the said aggregate net income of the company;

(b) where the company came into existence in the last year but one, or in the last, of the said accounting years, the references in this sub-section to the said accounting years shall be construed as references to the last two, or, as the case may be, the last, of those years.

(3) The assets of the company which are deemed to be included in the property passing on the death of the deceased by virtue of this section shall include any assets thereof which have been disposed of or distributed by the company at any time between the beginning of the first of the accounting years aforesaid and the death of the deceased, either—

(a) in or towards satisfaction of rights attaching to shares in or debentures of the company, or

(b) otherwise howsoever except as follows, that is to say, by way of sale for full consideration in money or money's worth received by the company for its own use and benefit, or in or towards discharge of taxes or rates or other liability imposed by or under an enactment, or in or towards discharge of a fine or penalty or of a liability for tort incurred without collusion with the injured party, including assets which have been so disposed of or distributed in a winding up, whether continuing at or completed before the death:

Provided that this sub-section shall not apply to assets disposed of or distributed by way of payments from which income-tax was deductable, or which were assessable to in-

come-tax, of amounts not exceeding in the aggregate, as respects payments made in any accounting year or in the period between the end of the last accounting year and the death of the deceased, the amount of the income of the company for that year or period.

(4) The Board may make rules—

(a) prescribing the class of companies which shall be deemed to be controlled companies and the class of dispositions or operations which shall be deemed to be transfers;

(b) prescribing the matters to be treated as benefits accruing to the deceased from such a company, the manner in which their amount is to be determined, and the time at which they are to be treated as accruing;

(c) prescribing the manner in which the net income and the value of the assets of such a company are to be determined;

(d) prescribing the manner in which the accounting year is to be reckoned;

(e) prescribing the manner in which the shares and debentures of such a company passing upon the death of the deceased are to be valued for estate duty;

(f) prescribing the conditions upon which and the extent to which transactions in the name of such a company shall be deemed to be bona fide transactions for full consideration; and

(g) generally for the purpose of checking the avoidance of estate duty through the machinery of such a company.

(5) For the purposes of section 31 the deceased shall be deemed to have had an interest in the property deemed by virtue of this section to be included in the property passing on his death.

17. Duty of company and officers of company to give information to Board on death of transferor.—(1) Where the deceased has made a transfer of property to a controlled company as described in section 16 the company shall be under obligation to inform the Board within one month from the date of the death of the deceased, of the death, of the fact that the deceased made a transfer of property to the company, and of the fact that benefits accrued to the deceased from the company, and every person who was an officer of the company at that date, or if the company has been wound up and dissolved before that date, who was an officer of the company at any time, shall be under the like obligation as respects such of the facts aforesaid as are within his knowledge, unless he knows, or has reason-

able cause for believing, that the information in question has already been given to the Board by the company or some other person.

(2) If the company or any such person as aforesaid who is under obligation by virtue of the preceding sub-section to give any information to the Board makes default in the performance of that obligation, the Board may impose upon the defaulter a penalty not exceeding Rs. 1,000.

18. Collection and incidence of duty under section 16.—(1) The following persons shall be accountable for the duty payable on the death of the deceased by virtue of section 16, namely:—

(a) the company;

(b) any person (other than a **bona fide** purchaser for full consideration in money or money's worth received by the company for its own use and benefit) who receives, whether directly from the company or otherwise, or disposes of, any assets which the company had, whether as capital or as income, at the death or at any time thereafter;

(c) any person who received any distributed assets of the company on their distribution:

Provided that a person shall not,—

(i) by virtue of clause (b), be accountable in respect of any assets for any duty in excess of the value of those assets, or

(ii) by virtue of clause (c), be accountable in respect of any assets for more than a part of the duty bearing to the whole thereof the same proportion that the value of the distribution of those assets bears to the principal value of the assets of the company passing on the death by virtue of section 16.

For the purposes of this sub-section the expressions "distributed assets" and "assets of the company passing on the death" do not include any distributed assets of the company which the deceased received on their distribution; and a person who, having received any distributed assets of the company, has died before the deceased shall be deemed to have been a person accountable by virtue of clause (c) of this sub-section.

(2) Where a company incorporated outside the provinces of India is accountable for any duty by virtue of the preceding sub-section or of this sub-section, every person who is a member of that company at the death shall also be accountable for a rateable part of that duty in proportion to the value of his interest in that company.

(3) A person accountable for any duty by virtue of this section shall, for the purpose of raising and paying the duty, have all the powers conferred on accountable parties.

(4) On a winding up of the company, sub-section (1) of section 230 of the Indian Companies Act, 1913 (VII of 1913), shall have effect as if there were included in clause (a) of that sub-section a reference to any duty payable in respect of assets of the company passing on a death by virtue of section 16 of this Act, and section 129 of the Indian Companies Act, 1913 (VII of 1913), shall have effect accordingly.

(5) The duty payable on the death of the deceased by virtue of section 16 shall be a first charge by way of floating security on the assets which the company had at the death or has at any time thereafter, and any part of the duty for which by virtue of clause (c) of sub-section (1) of this section any person is accountable in respect of any distributed assets shall be a first charge also on those assets :

Provided that nothing in this sub-section shall operate to make any property chargeable as against a **bona fide** purchaser thereof for valuable consideration without notice.

(6) Where any duty has been—

(a) paid by a person accountable therefor by virtue only of clause (c) of sub-section (1); or

(b) raised by virtue of sub-section (5) out of any distributed assets charged therewith;

that person or, as the case may be, the person who was entitled to those assets subject to the charge, may (without prejudice to any right of contribution or indemnity which he may have apart from this sub-section) recover the amount of the duty so paid or raised as aforesaid from any person who is accountable therefor otherwise than by virtue of the said clause (c).

(7) No part of the duty paid by the company shall be recoverable by it from any person on the ground only that he is entitled to any interest in, or to any sum charged on, the assets which the company had at the death of he deceased.

(8) The provisions of sub-sections (1) and (3) of section 48 shall not have effect in relation to the duty payable by virtue of section 16.

PART III.—EXCEPTIONS FROM THE CHARGE OF DUTY

19. **Foreign property.**—(1) There shall not be included in the property passing on the death of the deceased—

(a) immovable property situate outside the provinces of India;

(b) movable property situate outside the provinces of India at the time of the death except—

(i) in the case of settled property of which the deceased was a life tenant, if the settler was domiciled in any province of India at the time the settlement took effect;

(ii) in the case of any other property, if the deceased was domiciled in any province of India at the time of his death.

(2) The Board may make rules prescribing the manner in which the nature and the locality of different classes of assets shall be determined for the purposes of this section.

20. **Property held by the deceased as trustee.**—Property passing on the death of the deceased shall not be deemed to include property held by the deceased as trustee for another person under a disposition not made by the deceased or under a disposition made by the deceased more than three years before his death where possession and enjoyment of the property was **bona fide** assumed by the beneficiary immediately upon the creation of the trust and thenceforward retained to the entire exclusion of the deceased or of any benefit to him by contract or otherwise:

Provided that the property shall not be deemed to pass by reason only that it was not, as from the date of the disposition, exclusively retained as aforesaid if by means of the surrender of the benefit reserved or otherwise it is subsequently enjoyed to the entire exclusion of the donor or of any benefit to him for at least three years before the death.

21. **Interest failing before becoming an interest in possession.**—In the case of settled property where the interest of any person under the settlement fails or determines by reason of his death before it becomes an interest in possession, and one or more subsequent limitations under the settlement continue to subsist, the property shall not be deemed to pass on his death by reason only of the failure or determination of that interest.

Explanation.—Where property is settled by a person on himself for life and after his death on any other person, with

an ultimate reversion of an absolute interest or absolute power of disposition to the settlor, the property shall not be deemed to pass to the settlor on the death of such other person by reason only that the settlor being then in possession of the property as tenant for life becomes, in consequence of such death, entitled to the immediate reversion or acquires an absolute power to dispose of the whole property.

22. Property reverting to disponer.— (1) Where by a disposition of any property and interest is conferred on any person, other than the disponer, for the life of such person or determinable on his death and such person enters into possession of the interest, and thenceforward retains possession of it to the entire exclusion of the disponer or of any benefit to him by contract or otherwise, and the only benefit which the disponer retains in the property is subject to such life or determinable interest and no other interest, even contingent, is created by the disposition, then, on the death of such person, the property shall not be deemed to pass by reason only of its reverter to the disponer in his life time.

(2) Where by a disposition of any property any such interest as is mentioned in sub-section (1) is conferred on two or more persons either severally or jointly or in succession, sub-section (1) shall apply in like manner as where the interest is conferred on one person:

Provided that sub-section (1) shall not apply where such person or persons taking the said life or determinable interest had at any time prior to the disposition been himself or themselves competent to dispose of the said property.

23. Income of settled property acquired on death of spouse.—Where a husband or wife is entitled, either solely or jointly with the other, to the income of any property settled by the other under a disposition which took effect before (the commencement of this Act) and on his or her death the survivor becomes entitled to the income of the property (as distinguished from the property itself) settled by such survivor, estate duty shall not be payable in respect of that property until the death of that survivor.

24. Property passing by reason of a bona fide purchase for full or partial consideration in money.—(1) Subject to the provisions of sections 25 and 42 estate duty shall not be payable in respect of property passing on the death of the deceased by reason only of a bona fide purchase from the person under whose disposition the property passes, nor in respect of the falling into possession of the reversion on any lease for lives, nor in respect of the determination of any annuity for lives, where such purchase was made or such

lease or annuity granted for full consideration in money or money's worth paid to the vendor or grantor for his own use or benefit, or in the case of a lease for the use or benefit of any person for whom the grantor was a trustee.

(2) Where any such purchase was made, or lease or annuity granted, for partial consideration in money or money's worth paid to the vendor or grantor for his own use or benefit, or in the case of a lease for the use or benefit of any person for whom the grantor was a trustee, the value of the consideration shall be allowed as a deduction from the value of the property for the purpose of estate duty.

25. **Dispositions in favour of relatives.**—(1) Where a person dying after the commencement of this Act has made a disposition of property in favour of a relative of his, the creation or disposition in favour of the deceased of an annuity or other interest limited to cease on the death of the deceased or of any other person shall not be treated for the purposes of section 24 or section 40 as consideration for the disposition made by the deceased.

(2) If the deceased has made in favour of a controlled company a disposition which, if it had been made in favour of a relative of his, would have fallen within sub-section (1), this section shall have effect in like manner as if the disposition had been made in favour of a relative of his, unless, it is shown to the satisfaction of the Board that no relative of the deceased was, at the time of the disposition or subsequently during the life of the deceased, a member of the company.

For the purposes of this sub-section a person who is, or is deemed by virtue of this provision to be, a member of a controlled company which is a member of another such company shall be deemed to be a member of that other company.

(3) Where there have been associated operations effected with reference to the receiving by the deceased of any payment in respect of such an annuity or other interest as is mentioned in sub-section (1), or effected with a view to enabling him to receive or to facilitating the receipt by him of any such payment, this section shall have effect in relation to each of those associated operations as it has effect in relation to the creation or disposition in favour of the deceased of such an annuity or other interest.

(4) In this section—

(i) "Relative" means, in relation to the deceased—

(a) the wife or husband of the deceased;

(b) the father, mother, children, uncles and aunts, of the deceased; and

(c) any issue of any person falling within either of the preceding paragraph and the other party to a marriage with any such person or issue.

(i) Reference to "children" and "issue" include reference to illegitimate children and to adopted children.

(ii) Reference to "children" and "issue" include reference to illegitimate children and to adopted children.

(iii) "Annuity" includes any series of payments, whether inter-connected or not, whether of the same or of varying amounts, and whether payable at regular intervals or otherwise, and payments of dividends or interest on shares in or debentures of a company shall be treated for the purposes of this section as a series of payments constituting an annuity limited to cease on a death if the payments are liable to cease on the death, or the amounts thereof are liable to be reduced on the death, by reason directly or indirectly of the extinguishment or any alteration of rights attaching to, or of the issue of any shares in or debentures of a company.

(iv) "Associated operations" means any two or more operations of any kind being,—

(a) operations which affect the same property, or one of which affects some property and the other or others of which affect property which represents, whether directly or indirectly, that property, or income arising from that property, or any property representing accumulations of any such income; or

(b) any two operations of which one is effected with reference to the other, or with a view to enabling it to be effected or to facilitating its being effected, and any third operation having a like relation to either of those two, and any fourth operation having a like relation to any of those three, and so on;

whether those operations are effected by the same person or by different persons, whether they are

connected otherwise than as aforesaid or not, and whether they are contemporaneous or any of them precedes or follows any other.

26. **Effect of new or increased rates of duty on certain prior sales and mortgages.**—Where an interest in expectancy in any property has, whether before or after the commencement of this Act, been **bona fide** sold or mortgaged for full consideration in money or money's worth, and the rates of estate duty in force in the case of a person dying when the interest falls into possession are higher than the rates in force, if any, in the case of a person dying at the time of the sale or mortgage, then—

(a) no other duty on that property shall be payable by the purchaser or mortgagee when the interest falls into possession than the duty, if any, which would have been payable if the rates of estate duty applicable had been the rates in force, if any, in the case of a person dying at the time of the sale, or mortgage, and

(b) in the case of a mortgage, any higher duty payable by the mortgagor shall rank as a charge subsequent to that of the mortgage.

27. **Settled property in respect of which since the date of the settlement estate duty has been paid on the death of the deceased's spouse.**—If estate duty has already been paid in respect of any settled property since the date of the settlement, on the death of one of the parties to a marriage, the estate duty shall not be payable in respect thereof on the death of the other party to the marriage, unless the latter was at the time of his death, or had been at any time during the continuance of the settlement, competent to dispose of such property, and, if on his death subsequent limitations under the settlement take effect in respect of such property, was **sui juris** at the time of his death, or had been **sui juris** at any time while so competent to dispose of the property.

28. **Reduction of estate duty in the case of double taxation.**—Where any property is liable to estate duty under this Act and also, by reason of the same death, to a corresponding duty under the law of any reciprocating territory to which this section applies, the former duty shall be reduced in the following manner, namely:—

The property shall in the first instance be assumed to be liable only to the higher of the two duties; this higher duty shall then be divided between the provinces of India and the reciprocating territory in proportion to the un-

reduced duties leviable in each; and the share of the provinces of India resulting from such division shall be deemed to be the duty due in respect of that property under this Act.

Explanation.—"Reciprocating territory to which this section applies" means any part of His Majesty's dominions which the Central Government may from time to time by notification in the official Gazettee declare to be a reciprocating territory for the purposes of this section.

29. **Allowance for quick succession to land or a business.**—Where the Board is satisfied that estate duty has become payable on any property consisting of land (not being agricultural land) or on a business (not being a business carried on by a company) or any interest in such land or business passing upon the death of any person, and that subsequently within five years estate duty has again become payable on the same property or any part thereof passing on the death of the person to whom the property passed on the first death, the amount of estate duty payable on the second death in respect of the property so passing shall be reduced as follows:—

Where the second death occurs within one year of the first death, by 50 per cent.;

Where the second death occurs within two years of the first death, by 40 per cent.;

Where the second death occurs within three years of the first death, by 30 per cent.;

Where the second death occurs within four years of the first death, by 20 per cent.;

Where the second death occurs within five years of the first death, by 10 per cent.:

Provided that where the value on which the duty is payable of the property on the second death exceeds the value on which the duty was payable of the property on the first death, the latter value shall be substituted for the former for the purpose of calculating the amount of duty on which the reduction under this section is to be calculated.

30. **Exemptions, reductions, and other modifications.**—The Central Government may by notification in the official Gazette make any exemption, reduction in rate or other modification in respect of estate duty in favour of any class of property or the whole or any part of the property of any class of persons.

PART IV.—AGGREGATION OF PROPERTY AND RATES OF DUTY

31. **Aggregation.**—(1) For determining the rate of estate duty to be paid on any property passing on the

death of the deceased, all property so passing in respect of which estate duty is leviable shall be aggregated so as to form one estate and the duty shall be levied at the proper graduated rate on the principal value thereof:

Provided that any property so passing, in which the deceased never had an interest, not being a debt or right or benefit that is treated as property by virtue of the Explanations to clause 13 of section 2, shall not be aggregated with any other property, but shall be an estate by itself and the estate duty shall be leviable at the proper graduated rate on the principal value thereof.

(2) Every estate shall include all income accrued upon the property included therein down to and outstanding at the date of the death of the deceased.

(3) Property passing on any death shall not be aggregated more than once nor shall estate duty in respect thereof be levied more than once on the same death.

32. New rates of duty to be according to Central Act.—The rates of estate duty shall be according to such scale as may fixed by an Act of the Central Legislature:

Provided—

(a) that no such duty shall be levied upon estates whose principal value does not exceed Rs. 1 lakh; and

(b) that by way of marginal adjustment, the amount of estate duty payable on an estate at the rate applicable thereto under the scale of rates of duty shall, where necessary, be reduced so as not to exceed the highest amount of duty which would be payable at the next lower rate, with the addition of the amount by which the value of the estate exceeds the value on which the highest amount of duty would be so payable at the lower rate.

PART V.—VALUE CHARGEABLE

33. Principal value how to be estimated.—(1) The principal value of any property shall be estimated to be the price which, in the opinion of the Board it would fetch if sold in the open market at the time of the deceased's death.

(2) In this section the following expressions have the meanings hereby assign-fix the price of the property according to the market price at the time of the deceased's death and shall not make any reduction in the estimate on account of the estimate being made on the assumption that the whole property is to be placed on the market at one and the same time:

Provided that where it is proved to the satisfaction of the Board that the value of the property has been depreciated by reason of the death of the deceased, the depreciation shall be taken into account in fixing the price.

34. Valuation of shares in a private company where alienation is restricted.—Where the Articles of Association of a private company contain restrictive provisions as to the alienation of shares, the value of the shares, if not ascertainable by reference to the value of the total assets of the company, shall be estimated to be what they would fetch if they could be sold in the open market on the terms of the purchaser being entitled to be registered as holder subject to the Articles, but the fact that a special buyer would for his own special reasons give a higher price than the price in the open market shall be disregarded.

35. Valuation of interests in expectancy.—Where an estate includes an interest in expectancy, estate duty in respect of that interest shall be paid, at the option of the person accountable for the duty, either with the duty in respect of the rest of the estate or when the interest falls into possession, and if the duty is not paid with estate duty in respect of the rest of the estate, then—

(a) for the purpose of determining the rate of estate duty in respect of the rest of the estate the value of the interest shall be its value at the date of the death of the deceased; and

(b) the rate of estate duty in respect of the interest when it falls into possession shall be calculated according to its value when it falls into possession, together with the value of the rest of the estate as previously ascertained.

36. Valuation of benefits from interests ceasing on death.—The value of the benefit accruing or arising from the cesser of an interest ceasing on the death of the deceased shall—

(a) if the interest extended to the whole income of the property, be the principal value of that property; and

(b) if the interest extended to less than the whole income of the property, be the principal value of an addition to the property equal to the income to which the interest extended.

37. Valuation to be made by the Board.—Subject to the provisions of this Act the value of any property for the purpose of estate duty shall be ascertained by the Board

in such manner and by such means as it thinks fit and if it authorises a person to inspect any property and to report the value thereof for the purpose of this Act, he may enter upon the property and inspect it at such reasonable times as the Board considers necessary.

38. Costs of valuation.—Where the Board requires any person to report on the value of any property for the purposes of this Act, the reasonable costs of such valuation shall be defrayed by the Board.

39. Board may accept and certify valuation when convenient.—The Board on application from a person accountable for the duty on any property forming part of an estate shall, where the Board considers that it can conveniently be done, certify the amount of the valuation accepted by the Board for any class or description of property forming part of such estate.

PART VI.—DEDUCTIONS

40. Reasonable funeral expenses and, with some exceptions, debts and incumbrances must be allowed for in determining chargeable value of estate. Exceptions.—In determining the value of an estate for the purpose of estate duty, allowance shall be made for reasonable funeral expenses and for debts and incumbrances; but an allowance shall not be made—

(a for debts incurred by the deceased, or incumbrances created by a disposition made by the deceased, unless, subject to the provisions of section 25, such debts or incumbrances were incurred or created bona fide for full consideration in money or money's worth wholly for the deceased's own use and benefit and take effect out of his interest, nor,

(b) otherwise howsoever except as follows, that is to say, by way of from any other estate or person, unless such reimbursement cannot be obtained, nor,

(c) more than once for the same debt or incumbrance charged upon different portions of the estate,

and any or incumbrance for which an allowance is made shall be deducted from the value of the property liable thereto.

41. Further exceptions.—Where a debt or incumbrance has been incurred or created in whole or in part for the purpose of or in consideration for the purchase or acquisition or extinction, whether by operation of law or otherwise, of any interest in expectancy in any property passing

or deemed to pass on the death of the deceased and any person whose interest in expectancy is so purchased, acquired, or extinguished becomes (under any disposition made by or through devolution of law from, or under the intestacy of, the deceased) entitled to any interest in that property, then in determining the value of the estate of the deceased for the purpose of estate duty no allowance shall be made in respect of such debt or incumbrance, and any property charged with any such debt or incumbrance shall be deemed to pass freed from that debt or incumbrance:

Provided that—

(a) if part only of such debt or incumbrance was incurred or created for such purpose or as such consideration as aforesaid, this provision shall apply to that part of such debt or incumbrance only; and

(b) if a person whose interest in expectancy in the property so purchased, acquired or extinguished becomes entitled to an interest in part only of that property, this provision shall apply only to such part of the debt or incumbrance as bears the same proportion to the whole debt or incumbrance as the value of the part of the property to an interest in which he becomes entitled bears to the value of the whole of that property.

42. **Further exceptions.**—(1) Any allowance which, but for this provision, would be made under section 40 for a debt incurred by the deceased as mentioned in clause (a) of that section, or for an incumbrance created by a disposition made by the deceased as therein mentioned, shall be subject to abatement to an extent proportionate to the value of any of the consideration given therefor which consisted of—

(a) property derived from the deceased; or

(b) consideration not being such property as aforesaid, but given by any person who was at any time entitled to, or amongst whose resources there was at any time included, any property derived from the deceased:

Provided that if, where the whole or a part of the consideration given consisted of such consideration as is mentioned in paragraph (b) of this sub-section, it is proved to the satisfaction of the Board that the value of the consideration given, or of that part thereof, as the case may be, exceeded that which could have been rendered available by application of all the property derived from the deceased, other than such (if any) of that property as is included in the consideration given or as to which the like

facts are proved in relation to the giving of the consideration as are mentioned in the proviso to sub-section (1) of section 15 in relation to the purchase or provision of an annuity or other interest, no abatement shall be made in respect of the excess.

(2) Money or money's worth paid or applied by the deceased in or towards satisfaction or discharge of a debt or incumbrance in the case of which sub-section (1) of this section would have had effect on his death if the debt or incumbrance had not been satisfied or discharged, or in reduction of a debt or incumbrance in the case of which that sub-section has effect on his death, shall, unless so paid or applied three years before the death, be treated as property deemed to be included in the property passing on the death and estate duty shall, notwithstanding anything in section 24, be payable in respect thereof accordingly.

(3) The provision of sub-section (2) of section 15 shall have effect for the purpose of this section as they have effect for the purpose of that section.

43. Debts to persons resident out of the provinces of India not to be deducted in first instance except from duty-paid property outside the provinces of India.—An allowance shall not be made in the first instance for debts due from the deceased to persons resident out of the provinces of India (unless contracted to be paid in any province of India or charged on properties situate within any province of India), except out of the value of any property of the deceased situate out of the province of India in respect of which estate duty is paid; and there shall be no repayment of estate duty in respect of any such debts, except to the extent to which it is shown to the satisfaction of the Board that the property of the deceased situate in the foreign country in which the person to whom such debts are due resides in insufficient for their payment.

44. Cost of realising or administering foreign property may be allowed for within certain limits.—Where the Board is satisfied that any additional expense in administering or in realising property has been incurred by reason of the property being situate out of the provinces of India, the Board may make an allowance from the value of the property on account of such expense not exceeding in any case 5 per cent. on the value of the property.

45. Duty paid in foreign territory on foreign property to be allowed for.—Where any property passing on the death of the deceased is situate in a territory outside the provinces of India and the Board is satisfied that by reason

of such death any duty is payable in that territory in respect of that property, the Board shall make an allowance of the amount of that duty from the value of property.

PART VII.—COLLECTION OF THE DUTY

46. Duty may be collected by stamps or otherwise.—Estate duty may be collected by stamps or such other means as the Board may prescribe.

47. Payment of duty may be accepted in prescribed Government securities.—The Board may prescribe that Government securities shall be accepted in payment of estate duty on such terms as it thinks fit.

48. Persons accountable, and their duties and liabilities.—(1) Where any property passes on the death of the deceased, every person to whom such property so passes for any beneficial interest in possession, and also, to the extent of the property actually received or disposed of by him, every executor, trustee, guardian, committee or other person in whom any interest in the property so passing or the management thereof is at any time vested, and every person in whom the same is vested in possession by alienation or other derivative title shall be accountable for the whole of the estate duty on the property passing on the death:

Provided that nothing in this section shall render a person accountable for duty who acts merely as agent or bailiff for another person in the management of property.

(2) Nothing in this section shall render liable to or accountable for duty a **bona fide** purchaser for valuable consideration without notice.

(3) Every person accountable for estate duty under the provisions of this section shall, within six months of the death of the deceased or such later time as the Board may allow, deliver to the Board and verify to the best of his knowledge and belief, an account of all the property in respect of which estate duty is payable.

(4) Where the person accountable knows of any property which he has not included in his account because he does not know its amount or value, he may state that such property exists, but he does not know the amount or value thereof and that he undertakes, as soon as the amount and value are ascertained to bring a supplementary account thereof and to pay both the duty for which he may be liable in respect of such property and any further duty payable by reason thereof for which he may liable in respect of the property mentioned in the original account.

(5) Where two or more persons are accountable, either in the same capacity or in different capacities, for estate duty in respect of the same property, their liability is concurrent.

49. Every person believed to be in possession to deliver statement of particulars of property as required by Board.—Every person accountable for estate duty, every company to which, in the opinion of the Board, a transfer of property has been made by the deceased as mentioned in section 16, every person who is or was at any time an officer or auditor of such a company, and every person whom the Board believes to have taken possession of or administered any part of the estate in respect of which duty is leviable on the death of the deceased, or of the income of any part of such estate shall, if required by the Board, deliver to the Board and verify, to the best of his knowledge and belief, a statement of such particulars together with such evidence as the Board may require relating to any property which it has reason to believe to form part of an estate in respect of which estate duty is leviable on the death of the deceased.

50. Penalty for wilful default.—A person who wilfully fails to comply with any of the provisions of section 48 or 49 shall be liable to pay a penalty of Rs. 1,000 or a sum equal to double the amount of estate duty, if any, remaining unpaid for which he is accountable, according as the Board may elect:

Provided that the Board shall have power to reduce the penalty in any particular case.

51. Executor to specify all chargeable property with affidavit of valuation.—In all cases in which a grant of representation is applied for within six months of the death of the deceased—

(a) the executor of the deceased shall, to the best of his knowledge and belief, specify in an appropriate account annexed to the affidavit of valuation filed in Court under section 191 of the Court-fees Act, 1870 (VII of 1870), all the property in respect of which estate duty is payable upon the death of the deceased and shall deliver a copy of the affidavit with the account to the Board, and

(b) no order entitling the applicant to the grant of representation shall be made upon his application until he has delivered the account prescribed in Sub-section (1) and has produced a certificate from the Board under section 53 or 56 that the estate duty payable in respect of the property included in the account

has been or will be paid, or that none is due, as the case may be.

52. **Estate duty when due and how and when to be collected.**—Estate duty shall be due from the date of the death of the deceased and shall be collected upon the account delivered under sub-section (4) of section 48 or clause (a) of section 51 or prepared under sub-section (3) of section 54, and amended or modified where necessary as provided in sub-section (1) or sub-section (5) of section 54; and interest at the rate of 3 per cent. per annum shall be paid on the duty from the date of the death up to the date of the delivery of the account or the expiration of six months after the death, whichever happens first.

53. **Duty to be paid or security for payment furnished for delivery of account and certificate to be granted thereupon.**—Upon delivery of the account under sub-section (4) of section 48 or clause (a) of section 51, the person delivering it shall pay to the Board, or furnish security to the satisfaction of the Board for the payment of, the estate duty, if any, payable in respect of the property included in the account, and the Board shall thereupon grant him a certificate that such duty has been or will be paid, or that none is due, as the case may be.

54. **Board's powers in respect of valuations.**—(1) If the Board is of opinion that the person delivering the account has under-estimated the value of the property in respect of which estate duty is payable (whether by placing too low a value on the property included in the account or by omitting to include therein property that ought to have been included), the Board may inquire into the matter in such manner and by such means at it thinks fit and, if still of opinion that the value of the property has been under-estimated, may require him to amend the valuation.

(2) If such person does not amend the valuation to the satisfaction of the Board, the Board may move the High Court to hold an inquiry into the true value of the property:

Provided that no such motion shall be made after the expiration of one year from the date of delivery of the account under sub-section (4) of section 48 or clause (a) of section 51.

(3) In any case where no account has been delivered as required by sub-section (4) of section 48 or clause (a) of section 51, the Board may cause an account of the property passing upon the death of the deceased to be prepared in such manner and by such means as it thinks fit and may call upon any person who in its opinion is accountable for the

payment of the estate duty in respect of the property to accept such account.

(4) If such person disputes his accountability or the correctness of the account, the Board may move the High Court to hold an inquiry into the matter.

(5) The High Court when moved under sub-section (2) or sub-section (4) shall hold or cause to be held an inqury accordingly and shall record a finding on the matters in issue. The Board shall be deemed to be a party to the inquiry.

(6) Any person authorized by the High Court to hold the inquiry may take such evidence on oath as he considers necessary and shall submit to the Court a report of the result of the inquiry together with the evidence taken by him and such report and the evidence so taken shall be evidence in the proceeding.

(7) The Central Government shall, within twelve months after the commencement of this Act and may thereafter from time to time, appoint a sufficient number of qualified persons to act as valuers for the purpose of this Act and shall fix a scale of charges for the remuneration of such persons and the High Court may refer any question of disputed value under this section to the arbitration of any person so appointed; and the costs of any such arbitration shall be part of the costs in the case.
shall be part of the costs in the case.

(8) An appeal shall lie to the Federal Court from any judgment of the High Court delivered on a motion made under this section in any case which the High Court certifies to be a fit case for appeal to the Federal Court.

Explanation.—"High Court" in this section means the High Court to which, or to a Court subordinate to which, an application for a grant of representation has been made, or whereon such application has been made, the High Court which would have jurisdiction to entertain such an application.

55. Grant of representation not to be delayed by Board's motion.—Where any grant for representation has been applied for, it shall not be delayed by reason of any motion made by the Board under section 54.

56. Certificate of payment of duty, and penalty for non-payment.—(1) Where the valuation is amended by the person accountable upon the Board's requisition under sub-section (1) of section 54, or is enhanced by the High Court upon the Board's motion under sub-section (2) of section 54, and in any case where the original valuation has been discovered to be too low, such person shall

within one month of the amendment or enhancement or discovery pay the deficit duty which is payable in respect of the property upon the amended or enhanced or full valuation and the Board shall thereupon grant him a certificate accordingly.

(2) Where the valution is reduced by the High Court on the Board's motion under sub-section (2) of section 54, the Board shall refund to the person accountable any excess duty paid by him and shall grant to him a certificate that the full duty payable in respect of the property has been paid.

(3) In any case where no account has been delivered as required by sub-section (4) of section 48 or clause (a) of section 51, the person who is called upon to accept the account prepared by the Board under sub-section (3) of section 54 shall, within one month of his acceptance or, as the case may be, of the final disposal of the motion made under sub-section (4) of section 54, pay the full duty payable in respect of the property and the Board shall thereupon grant him a certificate accordingly.

(4) If the person accountable does not pay the amount of the duty due from him under sub-section (1) or sub-section (3) within the period specified therein, he shall be liable to a penalty of Rs. 1,000 or a sum equal to five times the amount due according as the Board may elect.

(5) Where a person accountable for the estate duty in respect of any property passing on a death applies to the Board at any time and delivers and verifies a full statement to the best of his knowledge and belief of all property passing on such death and the several persons entitled thereto, the Board may determine the estate duty payable in respect of the property and on payment of that duty, the Board shall give him a cerificate accordingly.

57. Commutation of duty in respect of interests in expectancy.—The Board in its discription may, upon application by a person entitled to an interest in expectancy, commute the estate duty which would or might, but for the commutation, become payable in respect of such interest for a certain sum to be presently paid, and, for determining that sum, shall cause a present value to be set upon such duty, regard being had to the contingencies affecting the liablility to and rate and amount of such duty, and interest being reckoned at 3 per cent.; and on the receipt of such sum the Board shall give a certificate accordingly.

58. Assessment in complicated cases.—Where by reason of the number of deaths upon which property has passed

or of the complicated nature of the interests of different persons in property which has passed on death or from any other cause, it is difficult to ascertain exactly the amount of estate duty payable in respect of any property or any interest therein or so to ascertain the same without undue expense in proportion to the value of the property or interest, the Board, on the application of any person accountable for the duty and upon his giving to the Board all the information in his power respecting the amount of the property and the several interests therein and other circumstances of the case, may by way of composition for all or any of the duties payable in respect of the property or interest and the various interests therein or any of them, assess such sum on the value of the property or interest, as having regard to the circumstances appears proper, and may accept payment of the sum so assessed in full payment of all claims for estate duty in respect of such property or interest and shall give a certificate accordingly.

59. **Board may allow postponement of payment on terms.**—Where the Board is satisfied that the estate duty leviable in respect of any property cannot, without excessive sacrifice, be raised at once, it may allow payment to be postponed for such period, to such extent, and on payment of such interest not exceeding 4 per cent. or any higher interest yielded by the property, and on such other terms as it may think fit.

60. **Board may remit duty and interest outstanding after twenty years from death.**—If after the expiration of twenty years from a death upon which estate duty became leviable any such duty remains unpaid, the Board may, if it thinks fit, on the application of any person accountable or liable for such duty or interested in the property, remit the payment of such duty or any part thereof or any interest thereon.

61. **Forms.**—All affidavits, accounts, certificates, statements and forms used for the purposes of this Part of this Act shall be in such form and contain such particulars as may be prescribed by the Board and, if so required by the Board, shall be in duplicate and accounts and statements shall be delivered and verified on oath and by production of books and documents in the manner prescribed by the Board and any person who wilfully fails to comply with the provisions of this section shall be liable to the penalty mentioned in section 50.

62. **Recovery of duty and penalties.**—Any estate duty or deficit duty and any interest or penalty payable under

this Act may, on the certificate of the Board, be recovered from the person liable thereto as if it were an arrear of land-revenue by any Collector in any province of India.

PART VIII.—CHARGE OF ESTATE DUTY ON PROPERTY AND FACILITIES FOR RAISING IT

63. Estate duty a Crown debt and a first charge on property liable thereto.—Estate duty is a Crown debt and, subject to the provisions of section 18, shall be a first charge on the property in respect of which it is leviable after the debts and incumberances allowable under Part VI of this Act.

64. Private transfers of property void against claim of estate duty.—From and after the death of the deceased, any private transfer or delivery of any property passing upon the death by any person to whom it so passes shall be void against any claim in respect of estate duty enforceable under this Act.

65. Discharge from estate duty in certain cases.—A certificate granted by the Board under section 56 or section 58 shall discharge the property included therein and the grantee so far as regards that property from any further claim for estate duty, but shall not discharge any person or property from estate duty in case of fraud or failure to disclose material facts and shall not affect the duty payable in respect of any property afterwards shown to have passed on the death nor any further duty payable by reason thereof in respect of the property included in the certificate:

Provided nevertheless that a certificate purporting to be a discharge of the whole estate duty payable in respect of any property included in the certificate shall exonerate a bona fide purchaser for valuable consideration without notice from the duty notwithstanding any such fraud or failure.

66. Person accountable to be repaid by trustees and owners in certain cases.—If a person accountable under section 48 pays any part of the estate duty in respect of any property not passing to him, it shall, where occassion requires, be repaid to him by the trustees or owners of the property.

67. Facilities for paying duty or raising amount already paid.—(1) A person authorized or required to pay estate duty in respect of any property shall, for the purposes of paying the duty, or raising the amount of the duty when already paid, have power, whether the property is or is not vested in him, to raise the amount of such duty and any interest and expenses properly paid or incurred by him in

respect thereof, by the sale or mortgage of or a terminable charge on that property or any part thereof.

(2) A person having an interest in any property, who pays the estate duty in respect of that property, shall be entitled to the like charge, as if the estate duty in respect of that property had been raised by means of a mortgage to him.

(3) Any money arising from the sale of property comprised in a settlement or held upon trust to lay out upon the trusts of a settlement may be expended in paying any estate duty in respect of property comprised in the settlement and held upon the same trusts.

PART IX—MISCELLANEOUS

68. **Jurisdiction of Courts barred save as expressly provided.**—Save as provided in this Act, nothing done or in good faith purporting to be done by the Board under this Act shall be called in question in any Court.

69. **Discharge of functions of Board by officers and authorities empowered by the Central Government.**—(1) Then Central Government may by notification in the official Gazette empower any officer or authority to discharge the functions of the Board under this Act or the rules made under this Act in respect of any specified matter.

(2) Where under this Act or the rules made under this Act the opinion, belief or state of mind of the Board is relevant in any matter, the opinion, belief, or state of mind of the officer or authority empowered in respect of such matter under sub-section (1) shall be deemed to be that of the Board.

70. **Rule-making powers of the Board.**—Subject to the condition of previous publication, the Board may make rules not inconsistent with this Act. prescribing all matters which by this Act are required or permitted to be prescribed, or which are necessary or convenient to be prescribed for carrying out the purposes of or giving effect to this Act.

STATEMENT OF OBJECTS AND REASONS

The object of the Bill is to impose an estate duty on non-agricultural property to assist the Provinces to finance their development schemes by fortifying permanently their revenues and enabling them to improve inter alia the existing social services. In spite of war-time taxation, enormous private fortunes have been made during the war, aggravating

the great inequality which already existed. Apart from providing funds for the expansion of social services, there is manifest justification for the measure. It will be a step in the process of reducing the great disparities of wealth, which is a prominent feature of Indian economy, and will set the country moving towards a more equitable distribution of the national income.

2. Death duties in one form or another constitute an important element in the scheme of taxation of most progressive countries. In 1924-25, the Taxation Enquiry Committee considered the question of introducing them in this country and recommended the imposition of an estate duty by Central legislation. Before, however, the recommendation could be acted upon, the entire Indian constitution came under review, beginning with the appointment of the Statutory Commission in 1928 and ending with the passing of the Government of India Act, 1935. Under this Act, legislation on duties of succession in respect of property other than agricultural land falls in the Federal list and similar legislation in respect of agricultural land in the Provincial list. There is, however, a distinction between a succession duty strictly so-called and an estate duty. The estate duty is levied because property has passed by death and the duty is graduated with reference to the total amount of property so passing. The succession duty, on the other hand, looks not to the size of the estate left by the deceased, but to the size of the separate shares received by the beneficiaries and, as the windfall element increases with the distance of relationship to the deceased, it is often graduated further on that principle. The question, therefore, arose whether an estate duty of the kind levied in the United Kingdom and recommended for adoption in India by the Taxation Enquiry Committee was within the competence of the Legislature, Central or Provincial, under the constitution embodied in the Government of India Act, 1935. A reference was made to the Federal Court who, by a majority, expressed the opinion that such a duty did not fall within any of the Legislative lists. The statute was amended to confer power on the Central Legislature to levy an estate duty in respect of property other than agricultural land, the proceeds being distributable among the Provinces according to the principles to be formulated by a Central Act. The Provincial Legislatures can levy a similar duty in respect of agricultural land. This position has been maintained in the Government of India Act, 1935, as adapted by the India (Provisional Constitution) Order, 1947. A Bill to levy an

estate duty was introduced in 1946 in the Central Legislature but owing to the recent constitutional changes it lapsed.

3. The draft Bill largely follows the lines of the Estate Duty Acts of the United Kingdom so far as the charging clauses are concerned. The Estate Duty will be charged according to the principal value of all property which passes on the death of any person, whether by the disposition of the deceased or by a settlement made by others. The governing principle is that the title of the State to a share in the accumulated property of the deceased is an anterior title to that of the interest to be taken by those who are to share it.

So far as the machinery of assessment is concerned, the Bill is an adaption of the provisions of the Court-fees Act, 1870, dealing with probate duties levied in the shape of court-fees.

4. There are two matters which have been left out of the present Bill, namely, the distribution of the proceeds of the proposed duty amongst the Provinces and the rates of duty to be levied. The intention is to distribute the proceeds of the duty (after deduction of the cost of collection) amongst the Provinces. The exact basis of distribution is a question which will have to be considered in consultation with the Provinces concerned. When a decision is reached the result will be embodied in a separate Central Act. The rates at which the duty is to be levied will also be fixed from time to time by separate legislation. It is not possible to estimate even approximately, the probable yield of the new duty, as much will depend upon the rates in force for the time being.

R. K. SHANMUKHAM CHETTY.

New Delhi;
The 11th March 1948.

Notes on Clauses.

References to Finance Acts, the Succession Duty Act and the Law of Property Act are to the United Kingdom Acts on those names.

In the drafting of the Bill, including the interpretation clauses, clauses 2 and 3, the United Kingdom Acts on the subject have been followed as closely as possible so that the assistance of the United Kingdom decisions may be available.

Clause 2.—Sub-clauses (1), (2), (5), (6), (7), (8), (9), (10), (13), (14), (15) and (16) are derived from section 22 of the Finance Act, 1894. The **Explanation** to sub-clause (13) is derived from section 45 of the Finance Act, 1940.

Sub-clause (3).—From section 59, Finance Act, 1940.

Sub-clause (4).—It is contemplated that the rules made by the Board under section 16 (4) of this Act will correspond with the definition contained in section 58 of the Finance Act, 1940.

Sub-clause (11).—From section 69, Indian Succession Act, 1925.

Clause 3.—Clauses (a), (c) and (d) of sub-clause (1) are adapted from section 22(2) of the Finance Act, 1894. Clause (b) is new.

Sub-clause (2) is inserted to remove the possibility of doubt as to the scope of the provisions contained in Parts II and III of the Bill.

Clause 4.—From section 1, Finance Act, 1894.

See in this connection the definition of "passing on the death" in clause 2(14). The "passing" may be immediately on the death, as where **A** settles a fund upon himself for life, and then upon **B** absolutely. Or it may be after an interval or at any period ascertainable only by reference to death, as where there is a trust for accumulation for a term after **A's** death. The passing may be certain, as in the first example above. Or it may be contingent, as where **A** settles a fund upon himself for life, and then upon **B,** if and when he attains the age of 21 with accumulations. The passing may be original as in the first example above; or it may be by way of substitutive limitation, as where property is limited to **A** for life, remainder to **B** if living at **A's** death and in default (which happens) to **C.** In all these cases estate duty is chargeable on **A's** death.

Illustration.—A bequeaths a fund to **B** for life and on his death to **C.** Here **C** has an interest in the fund expectant on the death of **B,** and if he dies before **B,** this "interest in expectancy"—which is "property" by virtue of the definition in section 2(13) above—passes upon **C's** death as part of his estate. Estate duty is accordingly payable under this section. But the duty may be paid either at **C's** death or on the death of **B** when the estate falls into possession (see section 36). If the duty is paid at **C's** death, regard must be had to the fact that the interest passing is only an interest in expectancy and an abatement or allowance must be made in respect of **B's** life interest, reckoning his expectation of life according to the accepted tables of mortality.

If, however, it is decided to postpone payment until **B's** death, when the reversion falls in, its value as a reversion calculated as above must still be added to or aggregated with the rest of **C's** estate in order to determine the correct duty on the latter, and when the fund falls into possession by the death of **B,** duty has to be paid on its value at that date, the rate being ascertained by aggregation of such value with the value, at **C's** death, of the rest of his estate [re Eyre (1907) K. B. 331].

Clause 5.—From section 2(1) (a), Finance Act, 1894.

Illustrations.—1. Property comprised in a revocable gift is clearly property of which the donor is competent to dispose. Hence estate duty is payable on the property on the donor's death, although the gift may not have been

actually revoked. Similarly, property comprised in a settlement where the settlor reserves an unqualified power to revoke the trusts and declare new ones is chargeable to duty.

2. **A** devises a house to his son, subject to a power for **A's** wife by deed or will to charge on it a sum of Rs. 1 lakh. On the wife's death, estate duty is leviable in respect of this sum as property of which she has competent to dispose and this is so whether she exercised the power or not. See section 3(4).

3. Under section 109 of the Indian Succession Act, 1925, a gift by will to the testator's child is preserved from lapsing where the beneficiary pre-deceases the testator provided that the beneficiary leaves issue living at the testator's death. The gift takes effect as if the beneficiary had died immediately after the testator and the property devolves under the beneficiary's will or intestacy. It is therefore property of which the beneficiary was competent to dispose and is chargeable with estate duty in connection with his death as well as in connection with the death of the testator, subject to any allowance for quick succession [re Scott (1901) 1 K. B. 228].

Clause 6.—From section 2(1) (b), Finance Act, 1894.

Illustrations.—1. **A**, a Hindu widow, having a Hindu woman's estate in house property makes a gift of the property to **B**. The result is that **B's** interest ceases on **A's** death and a right to the entire property accrues to the reversioners. Therefore estate duty is payable on the entire property on **A's** death.

2. **A** and **B** are undivided members of a Hindu joint family governed by the Mitakshara school of law. Neither **A** nor **B** can dispose of his undivided interest in the joint family property by gift or will under the existing Hindu law. If therefore **A** dies undivided, it cannot be said that his interest is "property of which the deceased was at the time of his death competent to dispose". The case thus falls outside section 5, but clearly falls within the present section, because the deceased's interest in the joint family property ceases upon his death. In this case the benefit which accrues to **B**, assuming that **A** has left no widow or children, extends to the whole of **A's** interest and the whole of it is chargeable to duty if it is not agricultural land.

3. **A** by will gives an annuity of Rs. 500 to **B** charged on house property worth Rs. 1,200 per annum and the house property itself, subject to the aforesaid charge, to **C**. On **B's** death an annuity ceases and estate duty is therefore chargeable on the value of the benefit arising by the cesser. Thus if the house property is worth Rs. 24,000 at **B's** death the value of the benefit would be $\frac{500}{1200} \times 24000 =$ Rs. 10,000

See section 39.

4. **A** is entitled to an annuity of Rs. 800 charged on certain house property and on **A's** death an annuity of Rs. 200 per annum becomes charged on the property in favour of **B**. In this case, upon **A's** death the owner of the property is chargeable to estate duty in respect of the cesser of the whole of **A's** annuity of Rs. 800 and not merely the cesser

of Rs. 600 per annum which is the difference between the two annuities.

5. A fund is held on trust during the life of **A** to pay an annuity of Rs. 1,000 to **B** and the remaining income of Rs. 2,000 per annum to **A** and on **A's** death the whole income of Rs. 3,000 per annum is to go to **B.** In this case upon the death of **A** no estate, duty is payable in respect of the cesser of **B's** annuity of Rs. 1,000. Under the present sub-section we have to see what was the interest of the deceasd which ceased on his death and the extent of the benefit arising from the cesser of that interest. It is clear that in the case put **A's** interest was limited to Rs. 2,000 per annum.

Clause 7.—From section 2(1) (c), Finance Act, 1894. These gifts are dealt with in section 191 of the Indian Succession Act, 1925.

Clause 8.—From section 2 (1) (c), Finance Act, 1894, and section 59, Finance Act, 1910.

Clause 9.—From section 2 (1) (c), Finance Act, 1894, and section 59, Finance Act, 1910.

The right to possess under the terms of a gift is not possession; and it is payment, and not the obligation to pay, which confers enjoyment.

If the non-exclusion of or benefit to the donor extends to or overrides the whole subject matter of the gift, the whole is chargeable with estate duty. But where the gift comprises separate parcels of property and an interest is reserved to the donor out of one of those parcels only, that parcel alone is chargeable with the duty.

The benefit need not be reserved out of the subject matter of the gift, but may be secured only by the donee's personal covenant.

The words "contract or otherwise" must be construed in accordance with the **ejusdem generis** rule; they connote an enforceable arrangement, though not necessarily between the same persons as are parties to the gift. The arrangement must however be referable in some way to the gift.

Clause 10.—From section 43, Finance Act, 1940.

Illustration.—**A,** a Hindu widow, having a Hindu woman's estate in house property surrenders her estate to the reversioners two years before her death. The property in such a case cannot be said to pass to the reversioners on her death, since it actually passes to them two years before. Therefore section 4 does not apply. Nor does section 6 apply, because the widow had, in the circumstances, no interest ceasing on her death: it had ceased two years previously. But under sub-section (1) of the present section the property is deemed to pass on her death and becomes chargeable to estate duty.

Clause 11.—From section 2 (1) (c), Finance Act, 1894.

Clause 12.—From section 2 (1) (c), Finance Act, 1894.

In a true joint tenancy the interests of the joint tenants must be equal and identical in every respect. Any one of them can in his life time acquire full dominion over his share by severing the joint tenancy or he can dispose of it

as he thinks fit, in which event the joint tenancy will, so far as his share is concerned, be severed by that disposition. The unsevered share of a deceased joint tenant in the strict sense, although it accrues to the other joint tenants by survivorship, is in consequence property of which he was competent to dispose and liable to estate duty as such under section 5.

But the liability to duty may extend further, for where the deceased, having been absolutely entitled to property, has caused it to be transferrrd to or vested in himself and any other person jointly, the whole property is deemed to pass on the death of the deceasd for the purpose of attracting estate duty. If the deceased provided the property originally, it is sufficient to attracting estate duty in respect of the whole that the beneficial interest in a part shall have passed or accrued on the death. This is the strict legal position under the present section. In practice, however, certain concessions are allowed in England. If, for example, any legally admissible evidence exists to show that the intention of the transaction was to make the parties true joint tenants in every respect, and it is shown that the survivor, although he provided no part of the property, was nevertheless entitled to and in fact received a severed share of income, estate duty is claimed in connection with the death of the person who provided the property only on the share in which he was beneficially interested unless he dies within three years of the transaction.

Clause 13.—From section 2 (1) (c), Finance Act, 1894.

There must be an existing donee. The owner of a policy cannot, so long as he remains the owner, be regarded as keeping it up for the benefit of a donee to whom he subsequently assigns it. The liability to duty is independent of the existence of any obligation upon the insured to keep up the policy or of any arrangement between him and any other person in relation thereto.

Clause 14.—From section 2 (1) (d), Finance Act, 1894 and section 28, Finance Act, 1934.

The general purpose of this provision is to prevent a man from escaping estate duty by subtracting from his means, during life, money or money's worth, which, when he dies, is to reappear in the form of a beneficial interest accruing or arising on his death.

Clause 15.—From section 30. Finance Act, 1939.

The purpose of this provision is to extend liability to duty to annuities and other interests which, though not directly provided by the deceased, are in substance attributable to property derived from him.

Clause 16.—From section 42, Finance Act, 1940 and section 35, Finance Act, 1944.

Sub-clauses (1), (2) and (3).—The necessity for these provisions will be illustrated by the following example :

A is the owner of an estate (not being agricultural land) worth Rs. 12 lakhs including a residential house and of stocks and shares worth Rs. 8 lakhs. He forms a company with a nominal capital of Rs. 20 lakhs divided into 50,000

5 per cent. preference shares and 150,000 ordinary shares, all of Rs. 10 each. He sells the estate and the securities to the company in consideration for the shares, of which 50,000 ordinary shares are allotted to him and the rest to his wife and children. As part of the arrangement, he is appointed governing director for life at a salary of Rs. 50,000 per year and the residential house, whose annual value is Rs. 5,000, is let to him as governing director at a rent of Rs. 1,000 per year. On **A's** death more than three years later, estate duty would, but for the provisions of this section, be payable only in respect of the 50,000 shares which he retained. There was no gift to the company, for the company gave full consideration. The only gift was a gift of the shares and that gift was not the subject of any reservation. No estate duty would be payable in respect of the cesser of the salary, because **A's** interest therein was as holder of an office.

Sub-clause (4).—There are numerous provisions on this subject in the U. K. Finance Act, 1940 which it has been considered better here to relegate to rules. Provisions of this kind were first enacted in the United Kingdom in 1930, but they were found to be ineffective and had to be recast in 1940. A number of adjustments were again found necessary in 1944. These constant changes indicate the desirability of making the provisions flexible so as to meet new methods of evasion; hence their relegation to rules in the present Bill.

Sub-clause (5).—From section 52, Finance Act, 1940.

Clause 17.—From section 53, Finance Act, 1940.

Clause 18.—From section 54, Finance Act, 1940.

Clause 19.—From section 2(2), Finance Act, 1894 and section 24, Finance Act, 1936.

The rules of English law relating to the nature and the situs or locality of assets of an intangible nature are complicated and in some respects doubtful. For example, immovable property situate outside the United Kingdom, if it has become subject to a trust for sale under a British trust or rule of law, is deemed to be personal estate and the interest of the successor is deemed to be a British chose in action. Again, the property of which a deceased partner of a British firm dies possessed is regarded as personal and movable property, even though part of the property belonging to the firm is immovable, and the situation of the asset is primarily determined by the principal place of business of the firm. A simple contract that is deemed to be situate in the country where the debtor resides at the creditor's death. Debts due from the Crown are regarded as situate in the place where the document of title is at the time of the death of the deceased and so on. Under sub-clause (2) above the Board may adopt the English rules where they are clear and simple. Otherwise, simple rules may be made.

Clause 20.—From section 2(3), Finance Act, 1894 and section 59, Finance Act, 1910.

Illustrations.—1. **A** dies leaving property of which he was a trustee for **B** under a will left by **C**. The property is not chargeable to estate duty upon **A's** death.

2. **A** dies leaving property of which he was a trustee for **B** under a deed of settlement made by **A** himself not more

than three years before his death. The property is chargeable to duty, for otherwise any person could evade the duty by making such a trust shortly before his death and declaring thereby that he is a trustee for some named heir.

3. **A** dies leaving property of which he was a trustee for **B** under a deed of settlement made by **A** himself more than three years before his death, possession and enjoyment having been assumed by **B** immediately upon the creation of the trust and thenceforward retained to the entire exclusion of **A**. The property is not chargeable to duty upon **A's** death.

4. **A** dies leaving property of which he was a trustee for **B** under a deed of settlement made by **A** himself more than three years before his death, **B** having assumed possession immediately upon the creation of the trust, but being bound by an agreement to give **A** a share of the profits until **A's** death. The property is chargeable to duty upon **A's** death.

Clause 21.—From section 5(3), Finance Act, 1894 and section 48, Finance Act, 1938.

The **Explanation** is derived from section 14, Finance Act, 1896.

Ex hypothesi in the case put in the **Explanation,** the interest of the deceased in the settled property fails before it becomes an interest in possession and in view of the decision in **A. G. v. Wood** that an absolute reversion may be a limitation which continues to subsist, the **Explanation** is redundant, although such a provision was inserted in section 14 of the Finance Act of 1896.

Clause 22.—From section 15, Finance Act, 1896.

Illustrations.—1. **A** settles property on trust for **B** (usually a poor relation or an old servant) for life and then for himself absolutely. No duty is payable on **B's** death, if he dies before **A**.

2. **A** settles property on trust to pay an annuity thereout to himself and, subject thereto, for **B** for life, with remainder to **A**. Duty is payable on **B's** death, because it cannot be said that the only benefit retained by **A** is subject to the life interest.

3. **A** settles property on **B** for life, with remainder to **B's** children absolutely and in default, for **A** absolutely. **B** dies without children. Duty is payable, for the contingent interests of **B's** possible children were "other interests" created by the disposition.

4. **B** gives property to **A**, who then settles it on **B** for life with remainder to himself. Duty is payable on **B's** death, for **B** was competent to dispose of the property prior to the settlement.

5. As in Illustration 1, but **B** dies after **A** and the property reverts to **A's** heirs. Duty is payable on **B's** death, for the property does not revert to the disposer himself.

Clause 23.—From section 21(5), Finance Act, 1894.

Illustration.—**A** by deed dated 1940 settled property on his wife for life, and on her death on himself for life, with remainder to their children. The wife dies after the commencement of this Act, leaving **A** surviving. Estate duty is not payable on her death, though it will be payable on the

subsequent death of **A**. The exemption would not have applied if **A** had become entitled to the corpus on his wife's death.

Clause 24.—From section 3, Finance Act, 1894.

Illustration.—On the marriage of **A** and **B**, **A** the husband, partly in consideration of the marriage and partly in consideration of the transfer to him of certain shares belonging to **B**, settled certain house property upon himself for life and then upon **B** absolutely. Here the consideration is only partly in money or money's worth, namely, so far as it consists of the shares. Hence under sub-clause (2), the value of the shares, as at the date of the settlement, is to be deducted from the value of the house property, as at **A's** death in ascertaining the sum in respect of which **B** is to pay an estate duty.

Property **bona fide** transferred by the deceased for money or money's worth is not chargeable to estate duty. Although such a transfer might be made in anticipation of death, the consideration received in respect of it becomes the property of the deceased and as such is liable to duty. To subject to taxation both the property whose sale produces that money or money's worth and that money or money's worth itself would be in substance to impose double taxation on the same property. Hence the exemption in this clause. The exemption is to apply not only when the property is acquired for full consideration in money or money's worth, but also, to a proportionate extent, where part of the consideration is of that character.

Clause 25.—From section 44, Finance Act, 1940. The relaxations provided for in section 40, Finance Act, 1944, are covered by section 30 of this Bill.

Clause 26.—From section 17, Finance Act (No. 2), 1940.

Clause 27.—From section 5(2), Finance Act, 1894, and section 13, Finance Act, 1898.

Clause 28.—

Illustration.—**A** dies leaving movable property in a province of India, being domiciled at the time of his death in the United Kingdom. By reason of the situation of the property in such province, the unreduced estate duty on the property under this Act, is, say Rs. 2,000. By reason of the domicile of the deceased the same property is liable to an unreduced estate duty of, say, £600 in the United Kingdom equivalent to Rs. 8,000. Assuming that the United Kingdom is notified as "reciprocating territory", the reduced duty due under this Act is arrived at by dividing the higher of the two duties, namely, Rs. 8,000 between India and the United Kingdom in the proportion of 2,000: 8,000. The Indian share thus works out to Rs. 1,600 which is accordingly the reduced duty due in respect of that property under this Act. Under the existing law in the United Kingdom, section 20 of the Finance Act. 1894, being applicable to the provinces of India. the United Kingdom duty will be reduced by Rs. 1,600 so that the reduced United Kingdom duty will be the equivalent of Rs. 6,400, i.e., £480.

Clause 29.—From section 15, Finance Act, 1914.

Clause 30.—This clause is intended to cover, amongst others, the deductions and relaxations provided for in section

51. Finance Act, 1940, and sections 38 and 40, Finance Act, 1944. The following are some of the exemptions which, if considered desirable may be allowed under this clause;—

(a) Gifts made in consideration of marriage.

(b) Gifts proved to have been part of the normal expenditure of the deceased and to have been reasonable: e.g., where a well-to-do man makes allowances to his children amounting to perhaps a fifth of his income; on his death no claim for estate duty need arise in respect of payments made within 3 years.

(c) Gifts not exceeding a certain limit, say, Rs. 1,000.

(d) Gifts to the Crown.

[These four exemptions correspond to those conferred in the United Kingdom by section 59, Finance Act, 1910.]

(e) Property given for national purposes or to a local authority or to a University [See section 15(2), Finance Act, 1894 and section 40, Finance Act, 1931.]

(f) Government securities issued free of tax in certain circumstances. [See section 47, Finance Act (No. 2), 1915.]

(g) The property of a common seaman, marine, soldier, or airman who is killed or dies in the service of His Majesty. [See section 8(1), Finance Act. 1894.]

(h) Property not exceeding a certain limit passing to the widow or lineal descendants of members of His Majesty's Forces whether officers, non-commissioned officers, or soldiers dying from wounds received or disease contracted on active service. [See section 14, Finance Act, 1900.]

(i) Property not exceeding a certain limit passing on the death of any person proved to be due to injuries received by him during the present emergency and within twelve months before his death, being injuries caused by the operations of war. [See section 46, Finance Act, 1941.]

[In view of the exemption in proviso (a) to clause 32, no further special exemption under (g), (h), or (i) above may be necessary.]

(j) Pensions or annuities payable by the Government of India, to the widow or child of any deceased officer of that Government. [See section 15(3), Finance Act, 1894.]

(k) Property which has paid "probate duty" in court-fees under the Court-fees Act, 1870 to the extent of such payment.

(l) Property which has paid "succession duty", to the extent of such payment. [See, for example the Bijni Succession Act, 1931 (Assam Act II of 1931), under which the Bijni Raj has to pay a fee at every succession.]

(m) Property of the Rulers of Indian States.

(n) Interest in ancestral property passing on the death of a minor coparcener in a Mitakshara joint family who has a male ascendant living. [If a son is born in such a family, he acquires a right by birth in the ancestral property and if he should die within a few days, his interest in the property would pass back and would, unless exempted, be liable to duty.]

Clause 31.—From section 4, Finance Act, 1894, and section 12, Finance Act, 1900, and section 45(3), Finance Act, 1940.

Illustrations.—1. On the death of **A** the following properties pass:

(i) His free estate, immovable and movable, worth Rs. 1,00,000;

(ii) Property settled by his marriage settlement worth Rs. 1,50,000;

(iii) House property worth Rs. 2,00,000 settled upon him by his father by deed.

Now, if each of these properties were taken separately, the rate of duty might be, say, 3 per cent. for the first two and 4 per cent. for the third. But under the rule of aggregation they must all be added together to form one aggregated estate amounting to Rs. 4,50,000 and the rate for an estate of this amount might be, say, 6 per cent. Estate duty must be paid on each property at 6 per cent.

2. **A** dies leaving (i) Rs. 1 lakh in cash plus (ii) a policy on his own life for Rs. 1 lakh absolutely and irrevocably nominated from its commencement in favour of **B.** Estate duty is chargeable on (i) under section 4 and on (ii) under section 13, but the two cannot be aggregated because **A** had never an interest in (ii), the interest arising only upon his death.

Clause 32.—The clause leaves the rate of duty to be fixed by a separate enactment. The provision in clause (b) of the proviso is modelled on section 13(1), Finance Act, 1914.

Clause 33.—From section 7(5), Finance Act, 1894, and section 60 (2), Finance Act, 1910.

Clause 34.—This embodies the principle enunciated in paragraph 275 of Volume XIII, Halsbury's Laws of England, Second Edition.

Clauses 35, 36, 37 and 38.—From sub-sections (6), (7), (8) and (9) of section 7, Finance Act, 1894.

In connection with clause 36 attention is invited to the **Illustrations** under clause 4.

Clause 39.—From section 8(8), Finance Act, 1894.

Clause 40.—From section 7(1), Finance Act, 1894 and section 44(1), Finance Act, 1940.

Clause 41.—From section 57, Finance Act, 1910.

Illustration.—Property is settled on **A** for life with remainder to his only son **B. A,** when in failing health, purchases **B's** remainder at a fair price, which in the circumstances is nearly the full value of the property, giving a promissory note or mortgage for the amount. Upon **A's** death, the property goes to **B** as his only heir. But for the present section, the amount of the debt would fall to be deducted under section 43, although the property would have devolved upon **B** even without the purchase. By virtue of the present section however no such deduction is permissible.

Clause 42.—From section 31, Finance Act, 1939.

Clauses 43, 44 and 45.—From sub-sections (2), (3) and (4) of section 7, Finance Act, 1894.

Clause 46. The English provision relating to collection of the duty is contained in section 8 (1), Finance Act, 1894, which simply makes applicable to the collection of estate duty the existing law and practice relating to any of the duties leviable on or with reference to death.

Clause 47.- Adapted from section 34, Finance Act, 1917, and section 42, Finance Act, 1918.

The term "Government securities" is defined in the General Clauses Act, 1897.

Clause 48.—Adapted from section 8(3) and 8(4), Finance Act, 1894, section 16, Law of Property Act, 1925 and section 54(8), Finance Act, 1940.

Sub-clause (2).—See section 8(18), Finance Act, 1894.

Sub-clause (4).—See section 6(3, Finance Act, 1894.

Sub-clause (5).—See Halsbury's Laws of England, Volume XIII, paragraph 298.

Clause 49.—From section 8(5), Finance Act, 1894, and section 57, Finance Act, 1940.

Clause 50.—From section 8 (6), Finance Act, 1894.

Clause 51.—Adapted from section 8(3), Finance Act, 1894, and section 191 of the Court-fees Act, 1870.

Clause 52.—From sections 6 (4), 6 (6), 6 (7), 6 (8), Finance Act, 1894.

Clause 53.—Adapted from section 11 (1), Finance Act, 1894.

Clause 54. —Sub-clauses (1) and (2) are adapted from section 19H (3) and 19 H (4), Courtfees Act, 1870.

Sub-clause (3) and (4) are new.

Sub-clauses (5) and (6) are from section 19H (5) and (6) of the Court-fees Act, 1870.

Sub-clause (7) is adapted from section 10(6), Finance Act, 1894.

Sub-clause (8) is suggested by section 66A(2), Indian Income-tax Act, 1922, and section 19 H (7), Court-fees Act, 1870 except that for "His Majesty in Council" "the Federal Court" has been substituted in view of the enactment of the Federal Court (Enlargement of Jurisdiction) Act, 1947.

Clause 55.—Adapted from section 191 (2), Court-fees Act, 1870.

Clause 56.—Adapted from sections 19E and 19G, Courtfees Act, 1870, section 11 (2), Finance Act, 1894, and section 14, Finance Act, 1907. In the majority of cases, the procedure will be that the person accountable will first deliver an account under clause 48(3) and pay duty on the property included therein under clause 53. Usually, the account will not be a complete one, for it has to be filed within six months of the death and full details may not be available. [See clause 48(4)]. In fact, it may have to be filed as early as possible, if the interest due under clause 52 is to be reduced to a minimum. This preliminary account will serve as a notice of the death to the Board, so that the Board may, if necessary, start making inquiries under clause 54. At a later stage,

the persons accountable should be in a position to deliver a full statement, to pay the entire duty due, and to obtain a certificate of payment under sub-clause (1) or (5) of clause 56. In complicated cases, they can apply and obtain a certificate of payment under clause 58. It is only a certificate under clause 56 or clause 58 that discharges the property. (See clause 65.) A certificate under clause 53 suffices for a grant of representation, so as to enable the grantee as early as possible to get in all the property vesting in him and to submit a full inventory as required by section 317, Indian Succession Act, 1925, but such a certificate does not operate as a discharge for the purposes of clause 65.

Clause 57.—Adapted from section 12, Finance Act, 1894.

Clause 58.—Adapted from section 13, Finance Act, 1894.

Clause 59.—Adapted from section 8(9), Finance Act, 1894.

Clause 60.—Adapted from section 8(11), Finance Act, 1894.

Clause 61.—Adapted from section 8(14), Finance Act, 1894.

Clause 62.—Adapted from section 19J(1), Court-fees Act, 1870.

Clause 63.—Adapted from section 44, Succession Duty Act, 1853, and section 9(1), Finance Act, 1894.

Illustration.—**A** makes a gift of property to **B** and a year later **B** transfers it to **C** and **A** dies in the second or third year. In this case a charge for estate duty will attach to the property in the hands of **C**.

Clause 64.—Adapted from section 8, Bengal Public Demands Recovery Act, 1913.

Clause 65.—Adapted from section 11(2), (3) & (4), Finance Act, 1894.

Clause 66.—Adapted from section 9(4), Finance Act, 1894.

Clause 67.—Adapted from section 9(5), (6) & (7), Finance Act, 1894.

Clause 68.—Adapted from section 67, Indian Income-tax Act, 1922.

Clause 69.—Sub-clause (1).—Power has been given to the Central Government rather than to the Board, because in case the functions of the Board have to be entrusted to Provincial officers (e.g., Collectors), section 124 of the Government of India Act, 1935, will be available.

Sub-clause (2).—Adapted from section 4B (2), Australian Estate Duty Assessment Act, 1914—1942.

Clause 70.—Adapted from section 50, Australian Estate Duty Assessment Act, 1914—1942.

APPENDIX II

PRELIMINARY REPORT OF THE SELECT COMMITTEE ON THE ESTATE DUTY BILL, 1948.

[Constituent Assembly of India (Legislative)]

We, the undersigned, members of the Select Committee to which the Bill to provide for the levy and collection of an estate duty in the Provinces of India was referred, met on the 2nd of August, 1948, to consider the Bill.

2. At this meeting, the Honourable the Finance Minister who is in charge of the Bill, with the permission of the Chairman, proposed that the consideration of the Bill by the Select Committee be postponed till the next Budget Session.

3. One of the grounds urged by the Honourable the Finance Minister was that the Bill was intimately connected with another Bill, namely, the Bill to codify the Hindu law, inasmuch as **the application of the Estate Duty Act would be well nigh impossible so long as the joint family under the Mitakshara system continued to be recognised by law as a unit for purposes of taxation.** The levy of any duty on the death of a member of a Hindu coparcenary is foreign to the fundamental principle of coparcenary under the Mitakshara law. No individual member of such family can predicate that he has a definite share in the property. His interest is a fluctuating interest capable of being enlarged on deaths in the family or liable to be diminished by births. The provisions of the Hindu Code regarding succession or the structure of a joint family would have a considerable bearing as to how the duty should be levied on the death of a member of such family, and it was, therefore, urged that the consideration of the Bill should await the passing of the Hindu Code.

4. The second point urged by the Honourable Finance Minister in support of his proposal was that under clause 19 of the Bill immovable property situate outside the provinces of India is exempt and movable property so situate is also exempt in certain circumstances. This would mean the flight of capital to Indian States for investment in immovable and movable properties, unless the States also introduce similar legislation and bring their level of taxation

to that prevailing in the Provinces of India. The question of integration of fiscal policy of the States with that of the Government of India has been taken up, but it would be some time before the relationship of the States with the Centre and their fiscal obligations and rights are determined and stabilised.

5. The Honourable the Finance Minister also urged that the Finance Ministry would like to have further time to scrutinise the provisions embodied in the Bill, as further consideration has shown that certain provisions have been rather hastily drafted and without full examination. The Central Board of Revenue, which is charged with the duty of administering the Estate Duty Act, thinks that it should be given time to revise some of the provisions of the Bill.

6. We have given anxious consideration to the proposal of the Finance Minister. We realise that to a very large extent the points raised by him were present to the mind of the members of the Legislature when it passed the motion to refer the Bill to the Select Committee and therefore cannot be said to raise questions which are new. Nevertheless the Committee with the exception of one member Mr. Sidhva felt that the arguments advanced by the Honourable the Finance Minister in support of his proposition that the consideration of the Bill by the Select Committee be postponed are weighty and should be allowed.

7. Accordingly we have resolved not to consider the Bill clause by clause as we were bound to do. We therefore report that we have at this stage no report to make.

B. R. AMBEDKAR.
R. K. SHANMUKHAM CHETTY.
K. SANTHANAM.
T. A. RAMALINGAM CHETTIYAR.
SATYANARAYAN SINHA.
M. ANANTHASAYANAM AYYANGAR.
NAZIRUDDIN AHMAD.
S. V. KRISHNAMURTHY RAO.
SURENDRA MOHAN GHOSE.
*R. K. SIDHVA.
ROHINI KUMAR CHAUDHURY.
RAM SAHAI.
V. C. KESAVA RAO.

NEW DELHI;
The 9th August, 1948.

* Subject to a Minute of Dissent.

MINUTE OF DISSENT

There was sufficient time for the Ministry to study the points raised in the report between the time the Bill was introduced and the day Select Committee met.

R. K. SIDHVA.

NEW DELHI;
The 9th August, 1948.